UNITED STATES AGENCY FOR INTERNATIONAL DEVELOPMENT

COMMON MARKET FOR EASTERN AND SOUTHERN AFRICA (COMESA)

REGIONAL INVESTORS ROADMAP

FINAL REPORT

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Increasing Cross Border Investment in COMESA

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THE COMESA REGIONAL INVESTORS ROADMAP

1. Executive Summary

Introduction

The United States Agency for International Development (USAID) has commissioned Booz Allen Hamilton to conduct The Regional Investors Roadmap of COMESA. This study seeks to answer the question of how to increase cross-border investment in the COMESA Region. Based on these answers, it offers recommendations of what COMESA can do to improve the investment environment such that investors are more likely to expand their operations into other COMESA countries. In compiling this report, one factor was considered unmovable: market forces will ultimately dictate the amount and patterns of investment within the region.

The member States of the Common Market for Eastern and Southern Africa, (COMESA) during their meeting in Kinshasa in April 1999, resolved that the region should become a Common Investment Area (CIA). They further resolved that measures should be put in place to ensure its realization at about the same time as the COMESA Free Trade Area (FTA) in October 2000. Consequently, there is urgent need to address the many barriers that continue to stifle investments and trade in the region so in order to establish the CIA in fact as well as in theory.

The Regional Roadmap is a means to deal with these impediments, consisting of issues that are less obvious and more difficult to address than the typical issues associated with tariffs and legislated non-tariff barriers. It is a program designed to identify and remove regulatory and administrative barriers to investment and trade.

Methodology

We studied four industries in ten countries. Both the industries and countries visited were chosen in conjunction with the COMESA Secretariat and USAID. Countries were broken up into geographic regions of the North and South, with two industries studied per region. Studies were conducted in a hub-and-spoke fashion, with regional economic leaders Zimbabwe and Kenya serving as hubs in the South and North respectively.

The purpose of dividing industries by countries was to look for common themes within the same industry across jurisdictions, but in no way suggests the absence of a particular industry from a country. By holding the industry constant while changing the country, we could isolate those items that did not change across borders. By then holding a country constant while looking at two industries, and comparing the regional results, we could isolate those constraints that did not change with the industry. In the end, this approach allowed us to obtain results of region as a whole, while permitting the consultants to achieve the depth of study necessary to draw relevant conclusions.

Table 1.1 – Industries Studied by Country

	Steel	Clothing	Leather	Oil Seed
Ethiopia			X	X
Kenya			X	X
Malawi	X	X		
Mauritius	X	X		
Namibia	X	X		
Tanzania			X	X
Uganda			X	X
Zambia	X	X		
Zimbabwe	X	X		

We also compared and analyzed National Investor Roadmaps for common themes. National studies deal with domestic impediments to investment, without specific reference to the type of investment. The studies covered eight countries (Kenya, Malawi, Mauritius, Namibia, Swaziland, Tanzania, Uganda, & Zambia) over the past six years and identified problems regarding cost of investment, cost of doing business and risk.

It should be noted that the purpose of the study was to identify problems that COMESA and its Member States could address. By nature, this results in a study that appears "negative" because it fails to capture progress made to date, or to highlight successes that COMESA has achieved over the years. We have attempted to rectify this by pointing out successes where useful and appropriate, especially where COMESA programs from the past can serve as models for overcoming similar constraints now.

<u>Fundamental Assumptions</u>

A fundamental premise that structures the conclusions and suggests the recommendations is that investors' decisions are made solely on the basis of Return on Investment. Investors determine return on investment by analyzing four components, either explicitly or implicitly, as reflected in the simplified formula below. For COMESA, the greatest importance lies in the fact that governments can influence each, and thus influence return on investment.

$$\mathbf{ROI} = \mathbf{F}\left(\frac{\overset{1}{\textbf{Revenue}} - \overset{2}{\textbf{Cost}}\ \textbf{(Profit)}}{\overset{3}{\ }\ \textbf{Investment Cost}} \times \overset{4}{\textbf{Risk}} \right)$$

There are other components of the practical formula, including most notably time (to realize this return), but these four provide an excellent analytical framework for categorizing constraints to regional investment. Each of the four categories is influenced by a wide range of factors. The four components of Revenue, Cost of Doing Business, Investment Cost, and Risk are broken into environmental and governed factors in table 1.2.

The public and private sectors both want more investment but they differ on what that means. The public sector tends to focus on productive investment, generally characterized by high value fixed assets, such as buildings, machinery, or equipment. The private sector considers any sunk cost that is intended to generate a return as investment. Examples that represent investment to the private sector but rarely to public sector include: costs of travel, costs of communications, and legal fees for negotiating contractual arrangements with local counterparts.

Table 1.2 Four Investment Components and Driving Forces

Component	**Market Factors**	**Governed Factors**
Revenue	Competitiveness, Market size	Consistency in applying tariffs
Cost of Doing Business	Input costs (labor, transportation ,raw materials, utilities)	Regulations, taxation, access to market
Investment Costs	Land values, market research, equipment costs	Availability of Land, Communications, Tariffs
Risk	Threat of Competition, Exposure to Economic Changes	Dynamic Legal Environment, Strength of Commercial Courts

In addition to this disparity in views, most governments do not recognize that investors typically enter a market gradually. Usually they begin by selling or buying from their home country. After that they may establish relationships with local distributors or suppliers. Other intermediate steps may include establishing a distributorship, building a warehouse, and building an assembly plant. In most cases, at least one or more of these steps are preludes to the goal of the public sector of having productive capacity investment.

By failing to approach investment from an investor's standpoint, governments unnecessarily restrict their investment promotion activities to a small subset of investment types, but without including the process by which those decisions are made about those types. Governments must broaden their view of investment in order to attract more of the fixed asset investment they want. By discriminating against intermediate steps of investment, they reduce overall investment. But by improving the environment for all stages of investment, "high-end" investors will also be attracted.

Findings and Conclusions

The four industries studied provided many similar findings despite the differences in their characteristics. These characteristics are summarized in Table 1.3 at the end of this chapter.

Significantly, investors interviewed were reluctant to invest in additional COMESA countries. Many simply cited their lack of knowledge of opportunities elsewhere. Operations were small in most businesses: small enough that management could not afford to leave for the time it would take to set up a new business. Steel and steel products seem to be the industries most likely ready to expand.

It has been widely reported that Sub-Saharan African companies boast the highest profitability rates in the world, errantly suggesting that provides the greatest returns on investment when risk is taken into account. Investors perceive that investing in the region entails a high risk. In this case perception is reality. Because of this risk, companies only take on projects that have potentially very high returns on investment to cover those risks. They avoid the more mundane, low return projects. The perception of risk is greatly exacerbated by a lack of information regarding investment destinations.

> Business. It's all about return on investment. Think about it. There's a finite amount of money available. If it runs out, game over. And if you make a sizeable ... investment in your company, you'll want to see a return."
>
> IBM advertisement, *The Economist,* Sept. 22-28, 2001, p. 19

Regional and national roadmaps identified common problems. For example, it is very difficult to bring in foreign expertise other than top management to virtually any COMESA country. There are significant bureaucratic costs and delays associated with many different legally required government transactions. Serviced land is not readily available for investors in many countries.

In addition, we identified a number of issues related to the separate industries:

Leather: The market for final goods is primarily external. There is a distinct absence of foreign participation in the raw material processes. Producers are often unaware of the standards in the markets where their goods are sold, so that many revenue-enhancing techniques are not employed. There is tremendous overcapacity in higher value processes, particularly tanning.

Steel: The marketplace is local, but shortages in raw materials and capacity exist. High transportation costs create natural barriers to foreign competition. Information is sorely lacking from country to country. Major opportunities exist for local manufacturers to expand.

Oil Seed and Cooking Oil. The marketplace is local, with export potential limited to specialty seeds because production is completely consumed by local demand. Raw material production does not meet local demand for processed oils, which is met in great part through foreign imports. Heavily protected borders limit economies of scale, so that production capacity is underutilized. Markets are not yet regional

Clothing and Textiles: The influx of used clothing creates a dilemma for policy makers, which will become a regional issue. For some countries, the marketplace for locally made goods is almost non-existent. Most of these industries are labor intensive. The combination of productivity rates and costs make many countries uncompetitive on the world markets.

Recommendations

Governments should lower cost of investment by providing information. Investors interviewed understood little about other COMESA countries' marketplaces. There was a significant cost to acquiring information. In most cases it meant extended trips for management. Investors did not perceive that there would be a reasonable return on this type of investment.

Governments must positively influence revenues by establishing a level playing field and lowering cross border barriers. For the most part, companies' abilities to maximize revenues are predicated on their own ability to compete in the marketplace. Governments have a role to play in ensuring marketplaces remain fair. The biggest complaint came from accusations of duty and tax evasion. By reducing corruption at the borders, countries can improve the competitive environments in which their companies compete. In addition, restrictive practices limit the size of the market for both sales of products and purchases of supplies.

Governments must reduce the administrative costs of doing business. Bureaucracy adds significant costs to businesses. By limiting access to service infrastructures, governments have inadvertently raised costs of doing business. Government policies on land, labor, and utilities can profoundly affect the costs of operations.

Governments should reduce risk through consistent application of laws and policies. Transparent, predictable processes allow investors to quantify their risks. Consistent implementation of policies reduces non-market uncertainties.

COMESA has a vital role to play in improving the investment environment. From its regional perspective, COMESA can do much to bring about the changes necessary for the success of the Common Investment Area. A few possible actions include:

Cost of investment: COMESA can become a catalyst to spur the dissemination of information across borders. Possible roles include: finding investors to take disseminate information on a commercial basis; assist individual countries in disseminating information; distributing information directly; and establishing and implementing regional standards for administrative processes.

Revenues: Corruption reduces revenues by distorting the competitive environment. Traditionally, it has been dealt with as national issue, but the impacts are increasingly regional as economic integration goes forward. COMESA can lead efforts to deal with corruption from a regional standpoint and as an independent agent, particularly with respect to tariff evasion and inconsistent customs enforcement.

Cost of doing business: The Investor Roadmaps have shown best practices in many different areas for reducing administrative costs and burdens. If applied regionally, reforms will increase the attractiveness of regional investment. COMESA should continue its standardization programs and build common agreement regarding expatriate work permits; regional licenses (for goods and services); land acquisition, customs procedures; company registrations; and accounting practices, among others.

Risk: Predictable taxes, tariffs, and administrative approvals are essential, but some countries act capriciously. Providing jurisdiction for COMESA to hear appeals from damaging administrative decisions would create a stabilizing influence and establish regional standards.

One constraint that is less tangible but highly relevant was repeatedly noted in interviews: attitude. COMESA is the champion of reform in the Member States. One challenge is to change underlying attitudes from control of investment to facilitation of investment, so that government officials view investors as partners in development, not adversaries. COMESA can also help to increase understanding and broaden the definition of investment to include the entire range of investment stages, from marketing to building factories for export production. COMESA has already had numerous successes in changing the investment environment, but the work is far from over.

Table 1.3 – Industries Studied and Characteristics

	Steel	Clothing	Leather	Oil Seed
Market-place	Primary Local	Mostly Foreign	Foreign	Local
Cost of Transport	Very High	Low	Low	Medium
Protection	Not much	None	None	Consider-able
Value Added	Low	Low-High	High	Low
Market	Industry	Primary Consumer	Consumer	Consumer
Capacity	At Limits	Excess Capacity	Excess Capacity	Excess Capacity
Foreign Competitor	South Africa	Asia, SA	Europe, Asia	Asia
Market Opportunity	High	Low	Very Low	Medium
Upstream Value Add Opportunity	Low	Medium	High	Low

2. Introduction

The United States Agency for International Development (USAID) has commissioned Booz Allen Hamilton to conduct The Regional Investors Roadmap of COMESA. National Investor Roadmaps, in-depth studies that detail the steps required of an investor to become legally established in a country, have been conducted in eleven of COMESA's 20 Member States. These reports address the administrative and procedural barriers facing investment into these countries. Many Member States have made great strides in recent years to liberalize trade and investment policies at the macroeconomic level and have just begun to grapple with issues of public sector reform.

This study looks to answer the question of how to increase cross-border investment in COMESA. As nations improve their individual investment environments, more investors are attracted to serve foreign markets. However, investment still lags well behind as the individual Member States' marketplaces remain too small to attract large scale investment. COMESA has made major strides in reducing the economic barriers between members. This report seeks to identify those measures that are within the control of Member States' Governments to eliminate artificial barriers to regional investment.

1. Background

The member States of the Common Market for Eastern and Southern Africa, (COMESA) during their meeting in Kinshasa in April 1999, resolved that the region should become a Common Investment Area (CIA). It further resolved that measures should be put in place to ensure its realization at about the same time as the COMESA Free Trade Area (FTA) in October 2000. Consequently, there is urgent need to address the many barriers that continue to stifle investments and trade in the region as a basis for attainment of a CIA.

The Regional Roadmap is a means to deal with these impediments, consisting of issues that are less obvious and more difficult to address than the typical issues associated with tariffs and legislated non-tariff barriers. It is a program designed to identify and remove regulatory and administrative barriers to investment and trade.

2. Approach

The study of barriers to trade and investment in COMESA is a broad one. There are some general barriers that are applicable in most circumstances, but many barriers are specific to sub-region, country, and, in some cases, municipality. Barriers can be industry specific, project specific, and task specific.

The study of barriers can be directed to answer a great number of current issues within COMESA:

- What is needed to attract more investment into the COMESA region?

- What barriers must be addressed to increase cross-border commerce in COMESA?
- What barriers exist to production for export from COMESA member states?
- What barriers exist to cross-border investment?
- And many other possible issues.

Of course, for this report to be effective, it must be focused, particularly as far as practical, day-to-day barriers go. Administrative barriers, those encountered on a daily basis by investors, are only unearthed through focused interviews with investors, facilitators (transporters, customs clearing agents, and accountants to name but a few), and government officials.

COMESA is an institution that has aggressively analyzed and addressed many of the issues facing the private sector. Its declaration as a Common Investment Area comes as a result of its desire to attract foreign investors to invest in multiple member states. However, few of Member States' existing investors have taken multi-country positions in COMESA.

It should be noted at the outset that the Roadmap analysis, by its nature, looks for *currently existing* problems that investors encounter and that should be removed or reduced to improve the overall investment climate. Consequently, this document will take on the characteristics of a “negative” report by looking at how far a country has to go, not how far it has come. It does not capture advances, successes, and improvements made prior to the period of analysis. This is particularly relevant to the case of COMESA because of the number of very successful programs that have either taken place already or are in process. For example, instead of covering the remarkable transformation from dozens of customs forms to one single declaration document, this document captures investors’ current complaints about delays in processing. Rather than noting that the Yellow Card Insurance Scheme, which has replaced vexing and expensive national insurance requirements with a single insurance policy good across borders, the report concludes that there are still a few exceptions to the enforcement of the Yellow Card. The authors of this report have highlighted some of COMESA’s successes along the way. Even so, we recognize that the purpose of the study is to identify solutions, and in the course of doing so, many existing programs already implemented will appear to go unrecognized.

One of the most important points that a foreign investor looks for when choosing an investment destination is the degree to which the local investment community thrives. With so few local investors expanding regionally, foreign investors raise questions as to the viability of their multi-country investments. Therefore, COMESA must, as part of its extensive program to attract more investment and grow trade, address the questions regarding local investment expansion.

This study sets out to address the concerns of local investors when considering regional expansion. In order to examine these concerns, this report builds on the eleven National Investors’ Roadmaps that have been conducted over the past 5 years. In gathering information for this study, the consultants compiled data from the existing Roadmap research, interviewed firms, interviewed intermediaries that act on behalf of the firms in communicating with government (banks, freight forwarders, and truckers to name but a few) and interviewed representatives of the public sectors. In an effort to have a more focused output, the team selected 4 industries in consultation with the COMESA secretariat and conducted interviews in 9 countries in COMESA.

a. National Investors' Roadmaps

While the overall logistical and administrative environment for individual Member States has considerably improved over the past decade, it still falls short of what many investors have come to expect, and still presents formidable barriers to cross border investment. Some of the constraints – when looked at individually – may appear to be mere annoyances rather than binding constraints. However, when grouped together as a whole, these constraints can deter regional investment; raise the cost of doing business, and stunt private sector development in the country.

The approach to national investor roadmaps has been developed and refined in similar projects conducted by USAID in Bolivia, Chile, the Dominican Republic, Ghana, Hungary, Madagascar, Malaysia, Mongolia, Namibia, Tanzania, South Africa, and Uganda. At the core, the Roadmap Model is composed of 13 core processes divided into four process groups over two phases of investment, start-up and functioning. The four process groups include:

- **Employing** issues, including obtaining temporary and permanent residency permits for investors, securing employment permits for expatriates, and handling local labor relations
- **Locating** issues, including purchasing land, transferring deeds, developing land, and complying with environmental laws
- **Reporting** to government, including registering a business, acquiring incentives, applying for specialized licenses, and registering for and paying taxes
- **Operating**, which includes importing, exporting, acquiring foreign exchange, and repatriating profits

The Roadmap is presented largely from the perspective of a foreign investor. The investor's perspective is also useful because it allows the public sector to see how an individual agency's policies and practices affect a broader, multi-agency process. The Roadmap is relevant to local investors and foreign investors alike, who are subject to the vast majority of steps outlined. In addition, particular attention is given throughout the study to the small to medium-sized investors who may be disparately impacted by various regulatory procedures.

The first step of the process component is to document, in as much detail as possible, the various steps required of a new business to establish itself and begin operations, in full compliance with existing laws and regulations. The licenses or approvals required, their application procedures, and criteria for qualifications are all detailed. The fees or processing payments are noted, as are typical processing times for each step. In most cases these are average processing times reported by the agencies for projects with no unusual characteristics or problems. Actual processing times encountered by firms may well be significantly longer, and the analysis section of the Investor Roadmap reflects where the public and private sectors disagree on how long a given procedure takes. The annexes to the report include copies of all the principal forms required for each step at each agency, fee schedules, and relevant contact information. This has been done during the assembly of the individual investor roadmap documents.

Process components are followed by an analysis in which policy and procedural issues are identified and discussed, with recommendations for streamlining made where appropriate. The analysis section highlights areas of concern, notes disagreements between the government's perspective and the business community, and adds a contextual dimension to the report's treatment of procedural issues. Recommendations are based on the twin objectives of simplifying application procedures for investors while enhancing the ability of government to regulate and screen key information properly.

b. Industries Selected

The Roadmap approach emphasizes the viewpoint of the investor. Four vertical industries were selected in order to have a more focused approach. Each of these industries had all of the components of the vertical chain operating in Member States in one form or another. Industries selected had raw materials operations, semi-finished goods producers, finished goods producers, and marketplaces with traders and distributors.

In consultation with the COMESA Secretariat, the following four industries were selected:

<u>Steel</u>: Steel is unique of the four industries studied in that it was the only one in which demand outstripped supply. Steel has not had to fight with underpriced foreign imports, largely because of the costs of transport. Iron ore is mined in a few member states, rolled largely in Kenya and Zimbabwe, and most member states have steel products producers in one form or another. While there aren't large transportation manufacturers in the region, steel products manufacturers have markets in building products and spares. This industry probably represents the greatest opportunities for cross-border investment out of the industries studied.

<u>Cotton, Textiles, and Clothing</u>: Unlike steel, cotton, textiles, and clothing are three related industries that are well integrated with the world economy. While cotton is grown in many of the member states, it is generally sold on world commodity markets rather than used by textile firms. Textile firms often work with cotton bought on world markets, and export their products to Asia and South Africa. Clothing manufacturers often make their clothing from textiles purchased in Asia, often from man-made materials (and often from lower priced and inferior materials than are produced locally). Different countries

have different policies on a significant factor in the marketplaces: second-hand clothing. The presence of second-hand clothing makes the marketplace impenetrable for many manufacturers of clothing.

Leather and Leather Products: Similar to Textiles and Clothing in that much of the marketplace for the raw materials is outside the region, the market for new leather products is minimal at best. The focus in this study was the conversion of raw hides to semi-finished goods. Because of the size of the industries (mostly very small), it is not clear that significant advantages in scale lie in regional integration. However, significant opportunities for growth lie in the ability of raw material suppliers to improve their products.

Oilseeds and Cooking Oil: This industry represents the most basic need of each of the four industries studied, and includes the only participation of foreign multi-nationals. Because of its importance, it is also the most regulated of the four industries, with governments sometimes imposing crippling barriers to regional trade. Raw materials are brought in from outside the region to supplement the shortfall in local raw materials.

c. Countries Selected

In selecting countries to study, the Region was divided into imaginary divisions of north and south. In each of the divisions, two industries were studied. This allowed for greater focus for each industry. The divisions were:

Northern Countries (including Ethiopia, Tanzania, Kenya, and Uganda) – oil seeds and cooking oil; leather and leather products.

Southern Countries (including Mauritius, Zimbabwe, Zambia, Malawi, and Namibia) – cotton, textiles, and clothing; steel and steel products.

This does not imply that oil seed industries do not exist in Zambia, or that there is no steel industry in Kenya; just the opposite is true. However, the countries studied were thought to be representative of the whole, and by focusing interviewing teams on fewer industries, deeper results could be sought.

The regional exercise views investment from the perspective of companies already involved in multiple countries in the region. It also complements many of COMESA's activities in eliminating both tariff and non-tariff barriers by examining the constraints investors are facing that are not part of laws of member states.

The initial phase analyzed several key local and multinational industries within COMESA and tracked the main issues within the key group of countries (listed above) for each. At the conclusion of this task, the activity seeks to provide a plan of action endorsed by the Council of Ministers, to address barriers to regional investment. Where possible, the plan will also identify actions that can be taken "with the stroke of a pen" by Ministers of COMESA member countries. As a result of these actions, especially those that can be taken with immediate effect, this project will result in increased trade and investment in the COMESA region.

In order for COMESA to be seen as an attractive destination for foreign investment, change must not be considered a one-time activity. Therefore, this project seeks to result in the formation of a committee comprised of government officials and private sector representatives to address related issues as they arise. This forum will also be able to manage and address outputs of similar future studies.

3. Assembling the Findings

In the most basic of models, the decision to invest comes down to two main factors: The cost of the investment and the size of the return. This is an oversimplified model, as other factors invariably come into play including risk, company strategy and focus, and capacity issues. However, cost and return are typically the driving factors, and from a preliminary review of the findings, the primary cause for the lack of cross-border investment in the region.

Most investors noted the small market sizes within the various countries as limiting their potential returns. COMESA has taken a number of strides to increase the profitability of a company’s returns, including lowered tariffs, lower transport costs, and other measures which have an impact on the movement of goods and services around the region.

To a lesser degree, COMESA programs are also reducing some of the costs of investing. Examples of this are improved communications and the relaxation of visa requirements for COMESA country nationals. However, relatively speaking, there is still considerable room for decreasing the costs of investment.

In each investment decision, a threshold for return is set based on the cost of the investment. For example, a Zimbabwean firm will first measure the cost of an investment in Zambia. On the basis of this cost, the Zimbabwean firm will set a minimum return, which is directly related to the volume of sales required for the investment to be profitable. If the firm feels that it will not achieve the minimum return, it will choose not to invest. This is sometimes determined using a scientific approach including market research and costing. More frequently, however, it is done by investors through feel and intuition, rather than calculation

The premise is, therefore, that if Member States can decrease the cost of investment, the required returns for the investment decrease in proportion. In many of the interviews conducted to the time of this writing, most firms do not see the markets to be big enough to justify the cost of investment. They see the returns to be too small to justify the cost of investment. By reducing the cost, COMESA based-firms would be more likely to invest.

a. Issues that Influence Returns

Market Size – This issue is the one most commonly mentioned in the areas of textiles and leather goods. Sub-issues include the purchasing power of the population, the availability of hard currency (in some countries), name brand recognition and the difficulty in establishing name brands, and competitive products.

For the last issue, competitive products, the issue of second-hand goods such as clothing and shoes has been particularly vexing for firms that had previously exported to some of the member states that now do not prohibit the import of second-hand goods. The report will not question the economics of allowing second-hand goods to be imported (or placing prohibitive tariffs on them) – indeed, these goods provide low-income purchasers the option to acquire high-quality, name-brand western products at very low prices. Currently, the cache of a Western name-brand product (and the lower price) is outweighing the downside of it having previously been worn in the minds of consumers. However, textile manufacturers report that second-hand goods have all but closed markets to them.

Costs of Transport – There are very few opportunities for manufacturers to use the sea to transport goods; most are required to use much more expensive road transport. In some cases rail is available.

The costs of road transport have fallen over the past several years due to various factors, including the increase in competition between road haulers. However, the cost for a Zimbabwean firm to export to Tanzania (by road and see) is in many cases significantly greater than for a firm shipping goods by sea from the Far East. As a result, many companies are only able to serve markets in immediate surrounding neighbors.

Corruption – The economic costs of corruption have been well documented in the many studies of the subject. Investors mentioned this subject repeatedly, but not in the context of the actual costs of the bribes required to clear goods at border posts. Investors' biggest concerns were centered on goods that entered the region from non-COMESA states without having the required tariffs collected. Many investors felt that they would be able to effectively compete given the free trade regime in COMESA – however, when foreign goods enter without having paid tariffs, the advantage disappears

Protection – The COMESA Free Trade agreement allows for limited exceptions to zero tariffs, including infant industry and exceptions. In the industries of Oilseed and Cooking Oil, very significant products in terms of economic impact, these forms of protection still exist virtually eliminating cross-border trade and investment. These forms of protection were not seen, however, in the steel and textile sectors.

b. Issues that Influence Cost

Costs of Distance Management – As most manufacturers in the region are not considered to be “large”, in many cases the Chief Executive Officer often manages production and serves as the lead sales executive. In order for the CEO to market the company’s products in foreign countries, he or she must leave the factory for a significant period of time. This represents an often-prohibitive cost to many trade missions.

This problem also arises in the case of companies that wish to expand their productive operations to other COMESA Member States. The few companies interviewed that were able to invest in other Member States were able to do so because members of management were available to relocate to the new facilities. However, this is a luxury that most companies interviewed did not have (excess management).

Some of the issues particularly germane to COMESA in this category include the cost of communications, the lack of information (next issue); the cost of living for expatriates; and the difficulties in acquiring expatriate work permits.

Lack of Information – many investors dismissed opportunities in other countries out-of-hand, despite never having conducted formal marketing studies. Information on even neighboring countries is often quite scarce. There are very few publications or newspapers that cover multiple countries (the East African being a notable exception). An investor in Zimbabwe or Mauritius has a very difficult time learning about current market conditions in countries such as Zambia or Namibia despite their proximity.

The cost of this lack of information is that investors must often spend a greater amount of time in a target market than should be necessary. This increases the costs, particularly in terms of time away from other activities including operations management and attending to other customers.

Another cost of the dearth of information to investors is the missed opportunities to participate in public and private sector tenders. Virtually all tenders released in the region are only available through local publications. This makes it extremely difficult for the smaller regional companies to participate in the bidding, often giving advantages to larger South African or Far Eastern companies that are financially capable of maintain a marketing presence in a country.

Bureaucracy – Companies based in COMESA Member States have no particular advantages in investing in other Member States. In many cases, regional companies are disadvantaged for several reasons including:

- Their lack of experience in foreign investment
- Their respective embassies and high commissions are less active in supporting firms from their countries than western embassies
- In some cases they are even discriminated against by civil servants, often being suspected of having less-than-genuine intentions or financially incapable of a proper investment.

The cost of bureaucracy can be crippling to cross-border trade and investment. However, from the interviews conducted, it appears that the perception of the bureaucracy is greater than the actual conditions. Most firms interviewed that had invested in other Member States reported that they did not face undue amounts of bureaucracy. However, firms that had not attempted to invest elsewhere cited bureaucracy as a key deterrent.

While investigating concerns of investors, it must be noted that many of them will raise concerns regarding barriers that may not be real, but only perceived. In fact, some of the answers to questions posed were factually inaccurate. However, these perceptions cannot be discounted. Investors will communicate these perceptions to other potential investors discouraging them.

In other cases, some investors continue to face problems that have been thought of as being addressed. In these cases, explanations include miscommunication by intermediaries (such as truckers and freight forwarders), under trained government officials, among other one-off events that may occur in the interaction between the government and the investor.

It is frustrating for a policy maker that has successfully implemented breakthrough programs to hear doubt, skepticism, and, in some cases, open dispute of the effect of such programs. However, it is the contention of the authors of this study that perception will drive investment in the short term more than the programs themselves. It was felt that greater value would come from interviewing a more investors than from determining whether these perceptions were accurate reflections of reality.

Therefore this study will focus on perception, and will make recommendations for both new programs and measures to address perceptions.

4. Report Structure

This report will identify the factors that are negatively impacting trade and investment in the region. Many of these factors are well known to COMESA – indeed, COMESA already has programs in place to address many of these issues. However, a comprehensive list will be presented, which will then be filtered into actionable issues on the basis of the following factors:

1) The issue is a significant barrier to trade and/or investment
2) The issue is within the capacity of the Member States to address without major costs being incurred.
3) The issue is one that affects the region and can be addressed at a regional level
4) The issue is not already being addressed by COMESA

Because this study was drawn on different industries, countries, and problems, the output has been generated as follows:

- Summaries of the previously conducted investor Roadmap exercises.

- Conclusions: grouped by industry, with the issues sorted by impact on the investment decision. This approach is supported with case studies in Appendix A

- Recommendations: grouped by issue type.

- Action Plan:

In Appendix A, this report presents case studies of fictitious companies that are proposed to be considering regionally investing. They are intended to be composite sketches of companies interviewed in the data collection phase.

Each of the case studies is used to illustrate each of the four components of an investment decision: sales and revenues, costs of doing business, costs of investing, and risk. While investors in each industry face issues in each of the four areas when making investment decisions, this report intends to provoke discussion on each of the four cases.

Appendix B presents detailed findings by country, representing the manner in which the research was conducted. Much of what is reported in this appendix represents the perceptions of COMESA investors at the time of the interviews.

3. CONCLUSIONS

This Roadmap analysis has resulted in the identification of numerous constraints to increased regional investment. These can be characterized as general issues affecting investment in any of the sectors studied (as well as other sectors not studied); issues related to the specific industries; and issues related to the individual countries. For the most part, the study does not focus on this third category – individual countries – except to the extent that country-specific constraints have an impact on the regional market. For example, the quality of roads in Kenya has an impact on the cost of imports and exports for Uganda and thus becomes a general issue affecting the region.

In keeping with the design of the Roadmap, the conclusions have been analyzed for relevant recommendations that the Member States or COMESA itself can effectively address through future actions. For example, international demand for oilseed products has an impact on regional investments based in Uganda, but there few actions that Uganda can take to address this directly. On the other hand, Uganda can address gaps in market information on oilseed.

The conclusions set forth below are addressed on a general and industry basis. They have been grouped in accordance with how the various constraints uncovered affect the four components of return on investment that go into an investment decision: costs of investment, revenues, costs of doing business, and risk. Thus this conclusion section preserves the industry-specific information encountered, which can be used for industry-specific recommendations for those interested in the industries while identifying those common factors affecting investment generally by looking at the problems encountered in different industries.

Certain issues have been universally accepted as preconditions for increased investment, in all industries, in all countries, and on all continents. Investors look for a stable political and economic environment, reasonable access to capital, a sufficiently trained and educated labor pool, basic (and stable) infrastructure, and access to a sufficient supply of inputs and market for outputs, among other things. Without these basic preconditions, it is still possible to attract investment, but costs and risks are higher, with potential return on investment and competitive potential – especially in a global marketplace – lower. Investors require a higher return on investment and stay away from those sectors that do not provide high returns. COMESA has been working diligently to better establish these preconditions, with numerous successes. The recent creation of the Free Trade Area cannot be underestimated for its importance in forwarding these goals. To the extent that COMESA and its Member States continue enhance any of these conditions, the investment climate will benefit all investment.

Two of the very basic conclusions of this Roadmap recommend policy shifts in the Member States in order to improve the investment environments. Making these shifts will be critical to the growth of the region and, as a result, the Member States within:

- Member States must focus on promoting profitability of firms within the region. This is a very significant mindset and practical shift (particularly those countries with formerly centrally-planned economies) in which profits are typically met with suspicion. The profits by firms within Member States will encourage increased investment and will attract competitors to the region. The recommendations flowing from the conclusions below are made to enhance profitability in the short term in order to lead to the long-term effect of growth.
- Member States should recognize that the process a firm conducts when it considers investment includes the critical stages of simply marketing and sales. In many of the countries in the region, investment is not recognized until fixed assets are present. It is recommended that Member States welcome any form of market exploration, particularly when it comes to firms from within the region.

This second point bears further discussion. Investors in each country and industry expressed frustrations and difficulties related to poor understanding of the investment process by government officials. This can be characterized as a definition problem: many policymakers appear to define investment as in terms of buildings, factories, expensive equipment, and transfers of very large amounts of capital or assets. For example, the Ugandan investment incentive program requires at least $300,000 in fixed assets for foreign investors to qualify for incentives ($50,000 for local investors), with qualifying assets including land and buildings, plant and equipment, office and laboratory equipment, data processing and communications equipment, and transport vehicles and storage vehicles. Small investors and those who move cautiously and incrementally are left out of this program.

Aside from the focus on size, these approaches miscalculate the investment decision process. Investors don't start with a factory, but build up after testing the market. They may begin by simply buying local exports or selling to local importers until a market is established. From there, they will begin to enter into more formal relationships, leading, perhaps to distribution or licensing agreements. As volume increases, they may find it worthwhile to rent or build warehouse space, or a small representative office. Only after fully getting to know the local market, including the supply of appropriately educated labor, infrastructure, input supplies, transport capacities and a host of other factors will they typically decide to invest large amounts of fixed assets. Each step along the way – from the first marketing trip to the first shipment of locally manufactured goods – is an investment. Investors consistently complained that only the last phase – high value fixed assets – were treated as investment for purposes of tapping into incentives or investment promotion assistance.

One final point on this theme bears noting. Most large capital investments, especially factories, rely on a supply of complementary small businesses that can support the large ventures through services, supplies, components and other functions. For example, General Motors Corporation (GMC), in Detroit, Michigan, relies on more than 1,000 small businesses in addition to its own thousands of employees. As a result, courting companies the size of GMC is most successful only when smaller investors are also active in the market. Investors do not generally feel that COMESA Member States are actively or properly courting these small "building blocks" of the investment environment. Interviews with immigration officials and policy makers often support this finding by suggesting their particular countries "have enough" of particular professions and industries and do not need additional foreign participants.

Specific conclusions are set forth below in the following order:

I. General (for all sectors and countries)
II. Leather and Leather Products
III. Oilseeds
IV. Textiles
V. Steel and Metal Products
VI. National Investors' Roadmaps

Each section follows the four-part focus established at the outset: improving profitability by lowering *Cost of Investment*, increasing *Revenues*, reducing *Costs of Doing Business*, and controlling or eliminating *Risks*. Not all issues fit neatly into a single category; for example, costs related to market information can be associated with the initial investment as well as the ongoing costs of doing business. For readability, we have addressed each issue primarily under one category.

I. GENERAL (for all sectors and countries)

A. Cost of Investment

Subsidies and Privileges. Domestic subsidies and infant industry privileges distort market signals and often lead to misallocation of resources or protection of inefficient and non-competitive industries. For regional investment, they keep new investors and competition out of the market, unless new investors can either obtain the subsidies themselves or produce at costs below the costs of their subsidized competitors. To the extent that subsidies are going to be allowed within COMESA, they should be reasonably consistent among COMESA Member States. This will provide for a more level "playing field" in which success is based on production and productivity and not nationality. The cost of skewing the market signals with competing subsidies is born by consumers.

Information Deficits. Investors lack information on opportunities within COMESA, while producers and exporters likewise lack information about markets within COMESA and abroad.

There is a substantial need for information sharing and linkages between COMESA Member States' economic promotion agencies. Cooperation is currently minimal, but with minimal investment could quickly provide much needed information flows, particularly for balancing supply and demand information in the region. In addition, these agencies are natural points for disseminating information on regional trade fairs, which, in any event, needs to be increased.

COMESA has recognized this need both in its planning and implementation of activities. There is a COMESA website in place along with the COMESA Information Exchange Network and TradePoint. These are not yet functioning optimally. Users complained of not getting viable leads and that information is not being updated frequently enough. In addition, not all members are submitting information on local tenders and investment opportunities so that information is limited. It would be useful to conduct an analysis of these services to determine how they can be improved, or whether they are viable.

Active promotion of COMESA products is needed. Within COMESA, most consumers prefer foreign products, especially at the high end. Some of this preference is based on quality differences, but not all. Many consumers are unaware of local products because they have not been effectively promoted in the region. In other countries, industry promotion has been very effective in sharing costs, and is often run by the private sector through industry associations. Of course, the promotion will only be effective if there is consistent quality behind the products being promoted.

> **Export Processing Zones (EPZs).** EPZs can provide economies of scale and direct incentives for export-oriented companies while providing jobs and investment for the local market. Kenya has been successful in attracting export industries to its EPZs, having recently landed a large investment in the clothing industry to take advantage of AGOA benefits. For the most part, however, EPZs are national efforts that focus on the use of local population and local resources close to multi-modal transshipment points (especially ports) for export to non-COMESA countries. On a regional investment scale, they may be less relevant, unless they are capturing cross border supplies of inputs or labor. (Leather processing, which can capture skins and hides from a multi-country base, is one example of and EPZ opportunity with a direct regional impact.) Because of this national character, we have not pursued EPZ issues to the same extent as others.

Cost of Capital. Weak financial markets and high costs of export and import financing were identified by a number of investors as constraints to increased regional investment. Problems included a lack of financing for consignment sales, inability to use equipment, inventory, land and other movable and immovable property for security in some countries, and high cost of interest, especially for sectors with cash flow delays.

To support trade, COMESA continues to support the PTA Bank, headquartered in Nairobi, Kenya. Started 1985, the Bank supports investment in COMESA with project finance loans of $200,000 or more, and trade finance lines of $250,000 or more. The PTA bank also supports lower lines of credit through credits to local banks. Despite the sound structure, however, the Bank and its programs do not begin to meet the overall need of the region. It would be useful to assess and recommend alternative programs for export financing as well as a detailed analysis of regional constraints to improved financial markets.

B. Revenues

Duty Drawbacks. Numerous investors complained that duty drawback systems are overly slow and cumbersome, so much so in some cases that investors will occasionally just give up and forego the repayment. This is not acceptable and raises the costs of doing business in the region, thus lowering investment while increasing prices to consumers. One reason for this problem is that authorities have sometimes attempted to combat abuses and fraud by complicating the application procedures rather than relying on audits and other enforcement tools to catch violators. While this is understandable, it is still unacceptable if the goal of the country is to increase trade and investment.

Harmonizing Investment and Tax Regimes. By generally leveling the playing field with regard to improved investment climates and tax incentives, the COMESA region can provide an environment for more investment based on comparative advantage. Much of the needed tariff rationalization is already underway. For incentives, it is unlikely, and perhaps unadvisable, to obtain complete harmony – European countries compete with each other for multi-national investors, and states and cities in the U.S. offer different incentives to attract new investment – but an overall positive investment framework will attract more investment generally to the region on a regional basis. The segmented environments and investment barriers between countries reduce overall investment, with most investments made only on a domestic basis.

> **Harmonizing Incentives**. In considering the Common Investment Area, considerable discussion within COMESA has been placed on harmonizing incentives across Member States. The idea is to reduce the possibility of competing for investors by escalating incentive packages. It is in the opinions of the authors that this discussion is premature. As long as (sometimes vastly) different tax regimes exist, the incentives cannot be isolated with a view towards harmony. COMESA covers a vast expanse of territory with different nations based on different economies and different basis of law.
>
> Worldwide best practice is now considered by the Foreign Investment Advisory Service, a joint venture of the World Bank to lower corporate taxes and eliminate all incentives. This eliminates the application of incentives, often a sore point for investors. The adjustment of tax regimes, already underway in COMESA, can be a lengthy process.

Privatization. Some COMESA Member States, such as Zambia, have aggressively pursued privatization and have thereby improved their investment environment. Others, such as Ethiopia, still have excessive government ownership of companies and land. State companies tend to be less productive, yet still drive out competition from their privileged positions by undercutting prices through government subsidies. This has a cross-border impact by eliminating opportunities for cross-border investment in countries with state-sponsored competition. A region-wide commitment to privatization will improve the environment for investment throughout. Worldwide experience to date has favored private sector production as the only long-term effective engine of growth.

Regional Cost and Quality. Variations of quality for inputs and final products were noted frequently as a problem in COMESA that can depress prices and damage reputation (further depressing prices) for products coming out of COMESA countries. COMESA's own goals and activities include work in quality upgrading and standardization, so that work in this area fits squarely within the COMESA mandate. In addition, lack of market information influences markedly different costs for the same or similar products in some areas. Needs can be addressed both issues through strong industry associations to work on behalf of their members and as counterparts or collaborators with COMESA. (A working example is the associations in the leather industry). Cost and quality problems are generally best handled with and through the private sector.

C. Costs of Doing Business

Customs and Duty Issues: General. Existing and potential regional investors noted constraints related to the import and export duties as well as problems with customs processes. Some of these constraints would have limited importance if the analysis were focused on the domestic market of an individual country, but become extremely significant due to the multiplier affect of having to deal with multiple occurrences within a single transaction. Some of the conditions will require mutual action of neighboring states to fully address the problem. COMESA has been addressing these issues at various levels with some solid successes over the years. Most notably, COMESA developed a single Customs and Excise Declaration (CED) form to replace burdensome documentation requirements, and is currently working to harmonize customs and tax administration at certain levels. Additional work is needed, however. These issues should be addressed on a collaborative, multi-party basis with the assistance and support of the COMESA.

Administrative Procedures. Great strides to reduce bureaucracy within the region, but cases of red tape still exist. In particular, investors noted the duplication of forms, information, and approvals when seeking to obtain register, bring in expatriate workers, and obtain licenses. While seemingly a small thing, the additional costs in terms of preparation, disputes, negotiations, and delays relating to unnecessary documents and procedures can be the deciding factor in the competition between regions for international investment. Ultimately these barriers raise prices for consumers in some of the world's poorest countries.

COMESA has already been very successful in reducing the documentation burden in the area of customs, having replaced most forms for most countries with a single declaration form. (Indeed, Zambia has gone from 34 forms to the single COMESA customs declaration.) In addition, the institution of the COMESA Yellow Card Insurance program has reduced redundant cross-border requirements for the transportation industry, although occasional violations of the system are still reported by transport groups, particularly in the south. Both of these show conclusively that COMESA can provide effective responses through targeted programs that improve the trade and investment environment. These successful initiatives can serve as models for building new programs to address other administrative barriers.

There is not yet an established mechanism for identifying and targeting particular administrative problems. For example, transport industry and freight forwarding associations are well poised to gather information about need for improvements in customs service, but there is no particular place where they can report their experiences and press for changes. In other areas, there may not even be associations yet to collect this information. While COMESA and ministries of some Member States provide information through web sites on what policies should be (by law), they do not provide for feedback from users about what is (in fact). This results in lost opportunities for identifying change while maintaining frustrations among investors. Some investors can press for individualized changes and exceptions, but this does not help. Instead, it actually worsens the impression that the rules of the game are not applied evenly.

Regionalizing Investment Procedures: Government leaders have aggressively pursued the reduction of administrative barriers within the region in order to improve their investment environments. In many cases, these reforms represent the most readily available forms of positive intervention. Upgrading economies, market sizes, and infrastructures are much longer-term initiatives and cannot be directly influenced.

There has been some discussion regarding furthering the reduction of administrative barriers by creating regional licenses and registrations. However, it is not clear that this measure will appreciably increase investment, as most investors did not note bureaucracy as their primary constraint to expanding within the region. In fact, the thought of such a body raised concerns of additional bureaucracy given another agency.

There is no worldwide precedent for regional registrations or licenses, although there is some precedent for the recognition of licenses granted within one member recognized in another (The European Union for example).

<u>Bonded Warehouses and Transit</u>. COMESA is already pursuing a bonded warehouse and transit system for the region, but the participants have not yet actively adopted it. Interest at this time seems to be high along the Mombassa-Kampala corridor, suggesting that this might serve as an appropriate pilot program, with emphasis on establishing the scheme in this one spot then rolling it out, based on success, to other corridors and regions.

<u>"Bottlenecks"</u>. Countries providing regional port access can either facilitate or constrain regional trade for landlocked countries with respect to their import and export needs. More often than not, investors complained of delays. Improvements have been made under COMESA, but there are still cost and timing concerns among investors.

Private Sector Treatment. Investors in all sectors complained of poor treatment by government officials with respect to a wide variety of functions, an understandable vestige of a past in which government focused more on control than facilitation of trade. This complaint existed on two levels: customer service generally, and technical capacity of officials to understand the needs of the business community, thus lowering the quality of their decision-making capacity when approvals were needed. This can be an important factor for investors deciding between different regions of the world – not just countries within a region – when looking for optimal investment conditions. COMESA's regional scope and influence make it a natural focal point for either offering or developing training programs that can be adopted by the Member States.

C. Risks

Consistency of Duties and Taxes. Member States do not yet consistently publish all necessary information regarding taxes, duties, fees, rules, and regulations, permitting unnecessary room for inconsistent and contradictory application of rules. COMESA has made important improvements in overall simplification of tariff bands and reduction of duties, especially among the adherents of the Free Trade Area, but investors still complain of inconsistent treatment and insufficient or contradictory information. These conditions reduce stability and predictability, and can enable some actors to manipulate the system to obtain non-competitive advantages. New investors will not be interested in entering the market in which the rules are unpredictable or unfairly applied.

These rules and duties should be published and updated regularly, both in hard copy for distribution at customs installations, tax authorities, and investment promotion agencies, and on websites, including the COMESA websites. Authorities must be bound by their most recently published rates and rules. Many investors feel, however, that when officials deviate from published practices or regulations, there is little recourse for appealing the decision economically.

COMESA may wish to consider whether complaints about or appeals from customs and tax duties should be handled at some point through COMESA itself, providing a higher level of jurisdiction and authority to bring about consistent enforcement within the region. While information collection and dissemination will help investors know which countries to choose or avoid, the entire region will benefit from bringing the "avoided" countries into compliance with the others.

As one example, Kenya was cited both by oilseed and leather investors as inconsistent in its applications of duties for importers from neighboring countries. Despite policy statements in favor of reduced and consistent tariffs, investors in the region noted numerous difficulties in obtaining predictable treatment based on published rules.

Country of Origin Enforcement. In several industries, investors and government officials noted serious problems with misuse of country of origin rules and labeling to obtain tax advantages in cross-boarder trading of foreign goods and products. One of the most widely cited examples was in the re-labeling of Asian vegetable oil products: importers in a country with relatively low import duties could re-label and re-export the products to COMESA neighbors under the more favorable regional duty structure. COMESA is already moving toward the most efficient solution for this problem through its program to create a single external border by 2004, thus establishing a single tariff for goods entering the region. In the meantime, however, COMESA may wish to consider a program for enforcing country of origin rules.

Smuggling and Rent-Seeking. A comprehensive analysis of the causes and effects of smuggling and rent seeking is needed to provide the basis for addressing these issues. As already noted, unnecessarily complex administrative procedures, such as customs clearance or building permit approvals, support rent-seeking and certainly encourage smuggling. In addition to simplification, COMESA Member States may wish to follow Mozambique's progress in privatizing its Customs function, to stabilize the system, stop discretionary rent-seeking, and increase revenues for the public treasury.

Organized, higher-volume smuggling (as opposed to the occasional bicycle through the bush) is generally a business decision – albeit illegal – based on costs, risks, and benefits. Where tariffs are relatively high, the risk of smuggling is covered by the benefit of avoiding high duties while being able to undersell legal competitors. There were a number of complaints of smuggling throughout the region, with a particular emphasis on the Great Lakes countries due to the porous coastline.

Many efforts to control smuggling focus on the enforcement side. Using the business, model, however, there is a second approach that can be very effective. In some cases, lowering tariffs reduces smuggling while increasing revenues and lowering cost to the consumer. In a famous analogous example, Brazil had very high income tax rates until the 1980s and very low compliance. Rather than attempt simply to increase enforcement, the Brazilian government chose to drastically reduce the tax rate of 30-50% to only 10%. In doing so, the costs and risks of being caught were no longer justified by the cost savings of non-compliance, so that compliance skyrocketed, bringing in more income tax revenues than

> **Corruption in COMESA:** Traditionally, corruption has been considered to be a national issue to be dealt with by the authorities within the country that it transacts. However, as COMESA Member States grow economically more dependent upon one another, the impact of corruption within one country can be felt across borders. As trade continues to increase, illicit transactions facilitating trade within one country could ultimately bring harm to another marketplace. The beginnings of this became apparent by investors in some Member States that were being hurt by corruption taking place in other Member States.
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> Corruption is an issue that has been examined at length worldwide and within COMESA Member States, and it is not the intent of this report to investigate the roots or the extent of regional corruption. However, it is recommended that COMESA begin taking steps to address corruption on the level it now manifests – as a regional issue.

ever before in Brazil's history. Similar market forces affect customs and smuggling and should be examined.

Private Sector Feedback. In most cases, COMESA Member States lack formal mechanisms for the private sector to provide input to policymakers about the impact of policies on the economy in general, or on certain business sectors. Occasionally, a representative body such as a chamber of commerce exists, but often this is only one group with limited ability to speak for a wide variety of economic actors. Although this survey uncovered numerous complaints and suggestions for changes, few of the investors interviewed felt they had meaningful recourse to policymakers to redress their grievances.

Coordination between Government Agencies. A number of investors noted that they had been promised various tax breaks and other incentives through Investment Promotion Agencies (IPAs) or other agencies but that the tax authorities did not understand or apply the incentives. Such inconsistencies lower investor confidence and are reported to other potential investors. These kinds of problems can be addressed by coordinating government services, and COMESA could develop programs to assist member states in improving coordination, including best practices and lessons learned as programs are instituted.

II. LEATHER AND LEATHER PRODUCTS

Leather and leather products have potential for regional investment and growth within COMESA, both for export and for the regional market. The environment for investment can be improved and enhanced through the joint and individual actions of COMESA and the member states through the recommendations actions set forth below. Two important issues should be noted and recognized by the relevant policy makers, however. One relates to the economic nature of the leather products industry, and the other to the trade-offs inherent in making policy choices that will support growth.

First, the existing leather industry is highly fragmented and decentralized through the various member states and thus fails to capture the economies of scale needed to make the leather products industry competitive internationally and regionally. Even the hides and skin export opportunities – which are the easiest to pursue – need some market integration across borders to improve earnings and capture value, but actual leather goods production will require some integration at the outset to lower costs and aggregate the skills needed to produce competitive products.

Each of the countries studied has high excess processing and production capacity, especially in the tanning industry. This historical tendency toward over-investment in activities not supported by the market has left the countries with much misplaced industrial capacity that cannot be used in the short-run, if at all. In other words, current market conditions mean that not all of these facilities can be run at capacity, and some of them will simply fail. This is unavoidable in the short and medium term.

By removing constraints to processing and production, those countries and companies with comparative and competitive advantages will capture a larger share of the market for intermediate and finished goods, while others will not. Current conditions dictate that not all of the existing investments can or should be utilized. In fact, the existing investments most likely to grow at first are the Kenyan companies doing cross-border business in regional skins and hides for their production and export business. This may have short-term political implications, but policy makers will do well to reduce constraints and let market forces determine where the most growth will take place.

Assuming that the current conditions favor integration through regional investment centered in Kenya, it should also be noted that not all – or even most – benefits in the industry will accrue to Kenya. First, the greatest potential for immediate improvement and growth is in the export of hides and skins. Each country can improve its earnings if quality and sorting are improved. Producers, traders and exporters will all benefit from the increased trade. Second, such growth can lead to increased investments by Kenyans or others in the value chain in other countries. Because of access to ports, Kenya certainly has an advantage in some respects, but any meaningful growth in the region will have to be on a cross-border basis.

A second important issue is highlighted by the case of Ethiopia's shoe industry. Ethiopian policy makers have chosen to support a local shoe industry by limiting the selection, quality, and price range available to all consumers. By forbidding the importation of substantially cheaper used shoes, the local industry can exist. The question is – should it exist based on a small, highly protected market? Note that the existing industry is not producing export quality shoes, and is able to sell primarily because they are the only suppliers in the market. It could be that these resources should be employed elsewhere, and would be but for the market distortions brought about by the import ban.

Other countries have chosen to permit their population to buy inexpensive, higher quality used shoes. Such shoes are attractive for a population with very little buying power, permitting them to use less of their very scarce resources on shoes in order to buy other items. Presumably, their buying patterns will change if they earn more (there is essentially no market for used shoes in countries that export them because people prefer new shoes when they can afford them).

There is little incentive to invest in leather production at this time, without tariffs or other restrictions that will drive up prices for most buyers within these markets. Even then, there is no guarantee the protected industry will be able to succeed once protections are reduced. Policy makers will need to weigh the costs and benefits very carefully in considering whether to impose import restrictions.

Conclusions for the Leather and Leather Products Industry

A. Cost of Investment

Rationalizing Import and Export Duties. Some of the existing tax schedules lowering revenues, profitability, and competitiveness at various points in the value chain for leather and leather products.

- Export Duties - Generally. Export duties always lower the domestic price for skins. With export prices are set by the international market, duties cannot be passed on to the end-buyer through higher prices, but must be pushed back down the value chain, to maintain required returns on investment, resulting in lower prices to skins producers. In general, lowering export duties will help the export industry to grow and increase the income of producers and others in the value chain. Of course, it also lowers government revenues from those duties, which is sometimes – but not always – recovered through increased volume of exports. Policy decisions will have to weigh the impact on the economy against impact on revenues.
- Import Duties on Inputs. Some countries do not adequately recognize the cost impact of duties on inputs used in export products. As a result, exporters are essentially taxed twice when adding value. For example, if chemicals needed for tanning are taxed as imports, then the tanned products are taxed as exports, the tanners costs are much higher and thus less price competitive on the export market. Many COMESA countries provide drawback benefits for inputs used in export industries, or simply reduce tariffs altogether for such imports. These policies are not region-wide, however, which reduces the attractiveness of investment on regional basis, encouraging investment only on a country basis.

Economies of Scale – Shared Effluent Treatment Plants. The relatively high expense and complexity of effluent treatment for tannery operations has proven very difficult for any single tannery to bear and maintain a decent return on investment. At this point in the development of the leather industry, help appears to be both needed and justified. This can come in several ways. First, private sector investors can be encouraged to cluster themselves physically around shared effluent plants, with the plants built by one or more of the tanners who then charge others for use to recover their costs. On the other hand, a government can underwrite the cost of the plant through direct grants, tax incentives, low cost loans and other mechanisms. Optimal solutions will depend on capabilities and resources of the investors and the governments involved. The long-term usefulness of such investment, however, will depend greatly on the market for locally finished leathers. Right now, quality of production in most countries is not up to international standards, so that local production actually reduces for the value in the world market. High cost investment for effluent treatment must be linked to a more extensive leather production strategy, including market development and extensive training.

Regional Centers for Collection and Grading of Hides and Skins. The hides and skins level of the value chain is currently hampered by a lack of collection centers. In well-functioning economies, it is normally not necessary for the government to assist with such items as collection centers or warehouses – these should be established by the private sector based on market demand. Assistance may be needed, however, to stimulate growth of this sector.

B. Revenues

Single Border. The tariffs on imports and exports between COMESA countries on hides and skins are almost unanimously cited as constraints to regional investment. Movement to the Free Trade Area has, in many cases, addressed this problem, both by eliminating internal regional tariffs and rationalizing external tariffs. Rrationalization and consistent, transparent, and predictable enforcement are needed to permit investors to identify costs and risks so that they are willing to increase their regional or local presence.

Improving Quality. Hide and skin grading standards are well established in the international market place and are the basis for export pricing. In general, COMESA producers are producing at unnecessarily low standards. International standards can be learned and applied throughout the region to capture the full potential value of hides and skins for export, and even for the domestic market. Fortunately, the leather industry has two very capable leather associations – LLPI and ESALIA – which provide a natural vehicle for establishing standards and developing training programs.

C. Cost of Doing Business

Development of Supporting Institutions. Improvement of local and regional conditions will require institutional support internally and across borders. Organizations such as the East and Southern Africa Leather Industry Association (ESALIA) are vital in gathering information on external and internal market conditions, disseminating information, and even training members. Such organizations are even stronger when their members include smaller associations representing sub-regions and sub-sets of the various actors in the value chain.

D. Risk

For the leather and leather products industry, no industry-specific risks were isolated. The industry is subject to the same general investment risks identified in the general comments.

III. OILSEEDS

The oilseed market in the COMESA region has two somewhat distinctive components – the seed itself and the vegetable oils derived from the seed. The demand for oils is extensive, with most of the population regularly using vegetable oils in preparation of foods. Because the population has low buying power, however, the demand is primarily for inexpensive oils, with little regard to type or source, and is very price sensitive.

Supply of oilseeds for oil production does not meet demand. COMESA is currently a net importer of vegetable oils. Most oilseeds produced locally are also consumed locally, with the significant exception of Ethiopia's export of specialty seeds for Asian markets. Existing crushing and refining capacity in the region is underutilized in all countries studied, with no more than half of the capacity in production. Because the local oilseed supply does not meet local demand, it must be heavily supplemented by imports.

The vegetable oil market for most COMESA countries is either dominated by or highly dependent upon vegetable oils from Asia, which are inexpensive and meet the local quality requirements. Currently, most COMESA countries have different duty structures for refined, packaged oils and raw oils, taxing the refined oils as a protection for the local processing industries. That is, oil importers who add value to the raw oils get a tax break. Because of the significant differences in tax structures, however, there is a great deal of deliberate mislabeling, so that much refined oil is brought in as crude, then packaged locally and resold without the duties, permitting unfair competition by those able to succeed in these schemes.

Common characteristics hindering greater investment in oilseed production include transport costs and low oil content. Much of the seed is produced by small farmers who live far from decent roads, making collection difficult and expensive. In addition, the seed often has low oil content, making it less valuable and thus less productive to farm. Another factor affecting price is the lack of an animal feed market. Where processors can sell the discarded, crushed seed as animal feed, this additional value improves the profitability of oilseed production. For most COMESA processors, this market is not available.

Oilseed is only one option for a farmer, competing with other uses of land and labor. Currently, maize provides a better return on labor for the average farmer, and thus the best lands and most labor are dedicated to maize farming instead of oilseeds. This, of course, makes perfect sense and is appropriate; it also has implications for potential growth of domestic oilseed production for local consumption. Unless improved seed varieties dramatically increase returns to compete with maize, farmers have no good reason to switch over.

Competition for land is a bit unusual. COMESA currently utilizes less than 20% of its available arable land for farming. In a market where land is at a premium, different products would compete for land use. In much of the COMESA region, this competition is based on the inability of farmers to expand landholdings through additional labor. That is, most agriculture is done by small farmers whose technology is limited, allowing them to farm only relatively small plots. More land is available, but they cannot take advantage of it. If they could improve production and productivity with better technology, they would be able to farm more land, and there would eventually be competition for land use. At this point, the competition is essentially only for labor use. The positive side of this situation is that there is plenty of potential for growth in the agricultural sector.

Recommendations for Oilseeds

A. Cost of Investment

Industry Associations. As the first two recommendations note, there is a substantial need for regional and local industry associations in the oilseed sector who can analyze the market, provide information, promote changes, and otherwise act to improve the profitability of the investment in this sector. No significant associations were identified in this survey that appear to be fulfilling this role effectively. In some cases, the larger investors may be willing to assist in the organization or support of producers' associations in order to help them increase their output for processing in the currently underutilized, local crushing and refining industry.

In addition to associations, the region would benefit greatly from linked commodity exchanges. Currently, there is little information shared between them, despite the proximity of the markets. By viewing COMESA as a single market and acting to create information exchanges based on that model, commodities exchanges can help to provide better market information for regional investors and producers to act upon.

B. Revenues

Improved Seed Quality. Across the region, producers are receiving lower value for their oilseed crops because they are using inferior seeds that either have low oil content or hard shells, both of which inhibit oil production. More productive seeds are available, but farmers are either unaware of them or do not have access to them. COMESA, working closely with industry associations, could have an immediate impact on the oilseed industry by helping to introduce improved seeds to the region and information on improved seeds.

Improved Crop Rotation Practices. Oilseed rotates quite well with pulses, which also have an international and domestic market. Many farmers are unaware of these simple practices, which lower the need for fertilizers to maintain soil quality. Again, by working through associations, COMESA and Member States can help bring value added to existing land and practices through dissemination of information to the producers.

Improved production and productivity of oilseeds and land dedicated to oilseed production are essential in increasing the supply of seeds to meet the economies of scale required for efficient, regional processing of seed into oil.

Analysis of Animal Feed Potential. Of the four countries studied, only Kenya had a sufficient demand for animal feed – mostly from the poultry industry – to capture the additional value available from crushed oilseed. One of the constraints to supplying the animal feed industry is the high cost of transportation in the region. Additional study may support the possibility of locating animal production close to crushing facilities to reduce transport costs and provide ready supplies of animal meal. Incentives could be provided for development of such clustered groupings, which would make investment in oilseed processing more profitable and attractive.

C. Cost of Doing Business

Transport Costs. As noted repeatedly for this sector and all others, transport costs related to poor road infrastructure are having devastating consequences for regional and local investment. Oilseed and its products are inherently bulky, and require substantial transport to reach the principle markets. The networks of roads and railroads in COMESA are simply not sufficient, and seriously limit the capacity for growth of regional investment. High transport costs favor decentralized, small capacity production of vegetable oils with low-end equipment at the village and town level. It is currently very difficult to capture the economies of scale that could be utilized if regional processors had better access to supplies.

D. Risk

Additional Analysis of Comparative Advantage. Although regional demand for vegetable oils is high, the demand is very price sensitive and is met extremely well through foreign suppliers. Indeed, much of the regional investment that currently exists services the import market for oils, including refining, packaging and distribution. Without this supply, problems of excess capacity would be substantially worse. This raises some serious questions regarding where efforts should be focused. Ethiopian producers are specializing in seeds for export, because the return on investment for export of specialty seeds is much higher than for producing oilseeds for the local market. This may be true for other countries as well, even with improved oilseeds.

Many of the producers currently supplying the domestic and regional markets may better utilize their resources by investing in export cash crops (like sesame seed for India) or switching to maize in order to increase income and purchasing power. This will further reduce oilseed for crushing in the local market, increasing utilization of foreign vegetable oils. This is a logical and appropriate economic decision. Unless return on investment in oilseed production can be improved to compete with maize and cash crops, farmers have no good reason to stay in oilseed. Solid economic and market studies are much needed to help governments and producers better understand the investment possibilities and consequences facing them. Investing now in areas of comparative advantage may change the short-term focus of the industry in favor of long-term development and growth.

Such a study may indicate that certain geographic locations are best suited for processing, and that regional investment could most profitably focus on cross-border distribution of centrally processed oils. In this case, ongoing government support of inefficient, underutilized processing plants may no longer be justified if the market will not support it. In other words, not all COMESA sub-regions can necessarily support the same processing plants in each country.

<u>Enforcement of Grade and Source Rules</u>. Fraudulent practices related to imports of oils are reported to be quite serious in the region. Asian refined oils are often imported as crude, in order to take advantage of the wide disparity in duties on the two. In addition, Asian oils are also repackaged once inside a country as COMESA origin, and then resold across borders with lower duty rates. In both instances, revenues are lost.

COMESA and its member states should examine the range of responses to this. One possibility is simply to enforce the rules more effectively, thus raising the overall cost of regional trade and lowering profitability while increasing state revenues. It is not clear what impact this will have on regional investment. Another possibility is to rethink the duty structure. When COMESA moves to a Common External Tariff, rules of origin will only be important upon initial import, and not in cross-border trade. In addition, studies on regional comparative advantage (suggested above) may indicate that the region would be better off reducing the disparity between imported and crude, thus shifting to an industry more focused on packaging and distribution of less expensive foreign oils instead of processing more expensive local oils.

IV. TEXTILES

The textile industry has several components, including fabrics and finished clothing, each with domestic and export markets. For finished clothing, the market is "universal" – that is, all people acquire and use clothing, so that the domestic market theoretically consists of the entire population. For textiles, the market is smaller, consisting of those who turn the textiles into finished products or sell them as fabrics. In both cases, external and domestic demand is potentially enormous.

Under these conditions, investment in the textile and garment industry could be quite profitable, especially with Africa's low labor costs. There is, however, fierce competition worldwide, with Asia dominating much of the industry both for textiles and finished goods. In addition, used clothing from Europe is very appealing to the low-income consumers of the COMESA region. Until recently, most African countries had highly protected textile and garment industries to shield them from this competition. This is no longer the case, and many COMESA-based companies have gone out of business. Only a few have been able to compete in the global marketplace, usually be carving out a specialty niche such as uniforms for local industries. Of these, many are at risk due to obsolete equipment that will put them at an increasing competitive disadvantage if no new investment is made.

<u>Recommendations for Textiles</u>

A. <u>Cost of Investment</u>

<u>Market Information</u>. Lack of market information plagues firms in the textile and garment industries. For new investment, information gathering often requires high-level managers and company officers to be absent from their work for significant periods of times while they investigate opportunities on the ground in other COMESA Member States. Regional and international trade fairs and exhibitions provide firm with good opportunities to make contacts, but the costs are high in terms of both expenses and absences from the office. Moreover, these fairs tend to be the principal point for information gathering, rather than just one of several information sources. As a result, participation in the fairs is degraded by insufficient information prior to arrival.

By providing firms with more information, COMESA can decrease the cost of investment and ensure that textile and clothing firms can achieve the revenue levels that are required to invest in exporting. This could take the form of an information clearinghouse or center within COMESA itself, or support and encouragement to private sector associations that can gather and provide information through their networks.

<u>Restrictions on Expatriate Labor</u>. Many COMESA countries impose significant restrictions on the ability of investors to bring their own personnel into a country on a

long-term basis or even to help start up a new operation. Official reasons for these restrictions usually are based on the belief that in economy with decent education and high unemployment there is no need to import “redundant” labor from other countries. For the investor, there is little redundancy. The skills being imported have to do with company culture, proprietary systems, highly technical skills dealing with very expensive equipment, and market information. While all of these can be learned, this learning takes time.

The immigration restrictions place unnecessary costs on investment. First, the process is often very difficult, fraught with irregularities or “facilitation” payments in addition to official fees. Second, timing is often uncertain, so that, for example, a company will import expensive equipment only to have it sit idle for months while immigration officials keep out the professionals needed to install operate and maintain. Third, investors must invest at artificially high rates in training in order to ensure that they have qualified replacements when the limited visas of their expatriate professionals run out.

These costs (and associated risks) reduce the overall profitability of investment. With the fierce competition in the textile and garment industry, this may be the deciding factor in an investment decision. As a result, countries who want to protect their local labor market by keeping out foreigners are actually keeping out the jobs that could have gone to their citizens. COMESA can provide a leadership in relaying this information to national policy makers and pressing for policy changes that permit investors to bring in the people they need.

B. Revenues

Competition from Used Clothing. The single most important factor in price competition in the COMESA region, and in all of Africa for that matter, is the used clothing industry. This industry presents policy makers with a dilemma. Used clothing provides relatively high quality clothing to low-income and underemployed consumers at affordable prices, well below the prices of new clothing. At the same time, this price competition means that very few local clothing manufacturers can compete within the COMESA market, costing the region numerous jobs as protective tariffs have been reduced.

Policy makers must balance the competing demands for local jobs through protective tariffs with consumer needs for low-priced quality clothing. The success of the choices made will be reflected at the election polls for the policy makers, so the decisions have another layer of consequences. COMESA can play an important role in helping to establish and enforce policies on these issues. Without the pressures of re-election by a national population, they can respond more to relevant market forces and deflect some of the political pressures for anti-market solutions.

C. Cost of Doing Business

No industry-specific costs were identified for textiles.

D. Risk.

Inconsistent Duties. A number of those interviewed in this sector complained of serious problems arising from inconsistent application of duties for imports and exports through the behavior of unscrupulous business people and customs officials. The impact of this is greater than lost revenues – it creates unpredictable risks in a highly competitive market that can mean the difference between success and failure. It can also keep investment out altogether because of the perceived risks involved.

Corruption has an impact on the region. National problems affect neighbors and affect the regional investment regime. As a regional organization, COMESA can bring countries together to address this as a regional issue.

V. STEEL AND STEEL PRODUCTS

Recommendations for Steel and Metal Products

As many of the problems faced by steel producers are results of short supply and not through an adequate marketplace, many of the recommendations are those aimed at encouraging further large-scale investment by reducing risk.

Manufacturers referred frequently to the large marketplace of Congo as a major opportunity, but all were, of course, concerned about the risks in the face of ongoing conflict. Firms realized that in order to compete with South African suppliers selling to markets such as Zambia, Malawi and Congo, they can get a significant transport cost advantage by establishing operations closer to the market. In order to induce firms to take on the risk of expansion, the following recommendations are applicable

E. Cost of Investment

Generally, the costs associated with starting up a steel products manufacturing operation are primarily fixed asset based, as opposed to government-imposed costs. Certain costs exist such as the need for an Environmental Impact Assessment, but these costs are necessary. Land is typically an important factor for an investor, but steel plants are in a position to use brown-field investments in abandoned factories, and do not need to go with the expenses of a full-blown startup.

Information: Investors require information to judge the opportunities and the risks of a project. In most cases, a startup operation will require significant costs in either visits from the home office or the services of a consultant to investigate the market on their behalf. It is recommended that COMESA compile a database on steel products marketplaces and investment opportunities in order to better facilitate cross-border investment.

Further, it is very difficult for manufacturers to learn of government and other large tenders in other countries. There is great expense in monitoring the government bulletins in other countries, as there is no clearinghouse for this type of information. The Internet would make an excellent resource to communicate tenders. It is recommended that COMESA either make efforts to attract a major provider of business information to the region to supply information to manufacturers at a fee or take on the responsibility itself.

Utility Hookups: Unless existing connection are available and adequate, many investor may face very lengthy periods of time to get utility connections. The utilities are typically constrained by available resources,

F. Revenues

Most investors interviewed did not complain about dumping or unfair advantages foreign firms have – this is likely due to the percent of the component that transport makes up in the price. Foreign competitors face the natural tariffs of high transport costs. This coupled with the shortage of supply of raw materials means that the prices are available for manufacturers to be profitable.

G. Cost of Doing Business

Many of the problems that steel manufacturers face are not endemic to this particular industry. Steel manufacturers face the same types of problems that every other manufacturer faces. The following recommendations are applicable, in many cases, to all industries.

Bureaucracy and paperwork: Many nations are reassessing their bureaucratic procedures in an effort to reduce submission requirements. It is recommended that COMESA monitor national efforts to reduce barriers in order to learn of best practices in the region and success stories.

Costs of Inspections: In many countries, inspectors require companies to subsidize costs associated with the inspections. This will likely be the case as long as license fees (which should typically be priced to cover the expenses associated with maintaining the license) are not held by the agencies but submitted to a central treasury fund. Usually budgets do not then cover the liabilities associated with the provisions of licenses. It is recommended that COMESA pursue policies in member states that fees paid for licenses remain in a fund needed to cover the costs of making inspections.

H. Risk

One of the largest barriers to cross border investment is the typical scale of the investment and the risks that are always associated with large investments. To the extent that these risks are related with governments applying laws or contract terms capriciously or inconsistently, COMESA could play an important role in stabilizing the environment by taking jurisdiction for appeals from claims against government. Many investors perceive – not always correctly – that courts or administrative bodies will be biased against them in any claims against the government. If they do not trust the government to uphold the law or the terms of any investment agreements, this will greatly influence their investment decisions. COMESA can restore trust in the regional legal environment through the COMESA Court of Justice by establishing the Court as an honest broker for public-private sector disputes.

VI. NATIONAL INVESTORS' ROADMAPS

In addition to the industry studies conducted for this Regional Roadmap, eight National Investor Roadmaps for COMESA countries were also analyzed: Kenya, Malawi, Mauritius, Namibia, Swaziland, Tanzania, Uganda, and Zambia. The National Roadmaps are designed to identify administrative barriers to investment in the subject country. These barriers, as a general rule, affect an investor's cost of investment, cost of doing business, and risks. They do not tend to uncover issues related to revenues.

The National Roadmaps identified dozens of administrative barriers to investment. The conclusions set forth below expand upon issues found in the regional study or identify issues not otherwise addressed in the Regional Roadmap but which nonetheless have an impact on regional investment.

Conclusions Related to Administrative Barriers

A. Cost of Investment

Restrictions on the Employment of Expatriate Staff. Respondents in the regional study noted problems in bringing in expatriate staff, but analysis of the National Roadmaps provided more specificity. Investors noted that in addition to the limitations on using expatriate staff, the process of approval is often complex, slow, expensive, and unpredictable. Many countries do not permit applications through their embassies and consulates abroad, only in country with immigration authorities, which is much more expensive for the investors. Some of the requirements are unnecessarily difficult, such as showing that no competent local employees could be found who could fill the position. Such restrictive practices affect regional investment by making it too difficult or expensive for investors to cross border if they need significant expatriate staff to implement the investment.

Excessive Labor Protection. National Roadmaps indicate that some countries have unnecessarily restrictive labor laws which raise the cost of investing without providing corresponding benefits. Keeping in mind that the purpose of investment is profits, and not employment, investors make employment decisions based on "bottom line" analysis. Restrictive labor policies in some countries are depressing employment. For example, some countries provide that if a laborer who is employed for more than three months becomes a permanent employee, subject to serious restrictions on dismissal. Investors deal with this by either dismissing employees before they become permanent, or hiring very few additional employees to meet increased seasonal demand to avoid becoming burdened with unproductive staff when the market turns down. On the whole, overly protective labor laws drive investors away, lower overall official employment, and limit the ability of investors to respond to cycles in demand.

Uncertainty and Expense of Obtaining Land. Whereas the Regional Roadmap identified land as a problem in Ethiopia due to state control of the land market and lack of private ownership, National Roadmaps indicate that there are more widely spread problems in obtaining land in the region. Most of these problems relate to three issues. First, land titles are often insecure because of unresolved competing historic claims to property, insufficient documentation of boundaries or prior ownership, or lack of respect in the past for land rights, as evidenced by government takings. Second, land transactions, which are complicated in most of the world, are extremely complicated in much of the COMESA region, with various agencies claiming jurisdiction and authority over transactions, including problems of traditional law that must be negotiated separately from modern law requirements. Third, many countries have gone through nationalization phases in which much land ended up in the hands of the state. The "privatization" process has often involved insider deals to politically connected individuals, thus creating a distorted market for land speculation. Recognizing that land is one of the most important assets for investment, much reform will be needed before the region can capture the quantity and quality of investment needed for sustained growth.

Overlapping and Conflicting Licensing Authority. National investors noted problems with two or more agencies that claimed overlapping authority in issuing licenses. These included municipal versus national authorities, and competing authorities within a given level of government. Investors were required not only to negotiate separately with each authority, but sometimes to act as the arbiter of conflicts between the two in order to get the license. This situation increases expenses as well as risks to investors. COMESA is addressing some of this issues with the 13 countries participating in the Regional Integration Facilitation Forum, but more work needs to be done.

Poorly Trained Officials. Many of the officials responsible for approving building permits, investment incentives, and other licenses or authorizations are said to be lacking the technical or business background needed to make meaningful, investor-friendly decisions. This results in delays, inappropriate denials, and increased costs and risks generally. The problem has been identified at two levels. First, civil service placements may not require the necessary set of skills for the people hired. Second, the unskilled officials do not receive the training they need after getting the job to be able to perform their duties properly.

B. Revenues

No specific revenue issues were identified.

C. Cost of Doing Business

Lack of Appropriate Skills in the Labor Force. Many investors have found that the educational or training system for the labor force does not adequately address the needs of business, so that graduates who should be ready to start at entry level positions have to be retrained or receive additional training before they reach entry level requirements.

This complaint is not about the lack of widespread education – which is a concern – but about the nature of the education being given. Very few schools or training institutes work with businesses to tailor their curriculum for the employment market, and many curricula have not been updated to reflect the shift to a market economy. As a result, businesses must invest in additional training or chase after the few (and therefore more expensive) properly educated workers.

Improper Utility Tariffs. Utilities in Africa generally are much higher than on other continents. To make the situation worse, many locales do not have proper mechanisms for measuring utility cost per customer (such as water or electricity meters) or systems for monitoring and removing illegal taps into the utilities. At times, utility companies simply charge based on an estimate of what they believe an investor uses. Lost revenues to the utility company are made up by overcharging those who can pay. Investors sometimes control costs by providing their own power systems, but this is not an efficient or cost effective solution to the problem. Utility regulation and reform is needed.

Unnecessary Delays in Customs Clearance. Investors report that even with improvements in documentation requirements, there are many customs officials who create delays in processing shipments due to lack of skills and education. In short, investors find that the officials are under-trained. Consequently, they increase waiting time, costs associated with documents, and misapply tariff rules. This also leaves room for corruption in order to "facilitate" payments. In addition, there is a tendency, as noted elsewhere, for government functionaries to treat their customers – the investors – as adversaries instead of partners in development.

Limited Sources of Short-Term Financing or Reasonable Interest Rates. Cost and availability of capital are recurrent themes throughout the COMESA region in all studies. COMESA, through the PTA Bank, has sought to address these needs, but demand has outstripped supply. One of the glaring gaps in the system is the lack of suitable secured lending regimes to meet the need for short-term financing on movable property, a foundation of economic growth. In addition, there is a lack of information about available resources (many investors are not familiar with PTA Bank) and about the numerous donor-supported programs in the region. A clearinghouse is needed for information on finance.

D. Risk

Lack of Transparency. This complaint arose in a number of contexts, but mostly with regard to denial of licenses, permits, and approvals. Investors regularly find that decisions are handed down based on factors they could not have known, or on factors that they do not get to know because the decisions are not written, or if written, are not reasoned. A frequent area of complaint was on immigration permits for expatriate workers. These kinds of unpredictable outcomes increase risk as well as expense for investors. COMESA is working to harmonize administrative practices, and will need to ensure that practices related to transparency are included in their program.

Unfulfilled Promises. Many investors have made decisions based on guarantees from Investment Promotion Agencies only to find that the revenue authorities, customs service, labor board, or immigration officials do not recognize the guarantees or do not interpret the law in the same way. This rude awakening does more than increase costs for the investor; it also drives away new investment. IPAs may need assistance from COMESA to pressure national governments into establishing predictability through enforceable incentives.

Perceived Bias in the Court System. Whether true or not, many foreign investors feel that local courts are biased against them, so much so that they are unlikely to receive a favorable judgment no matter what their case if it involves damage to a local national. This problem is universal – not just a regional issue unique to COMESA. Other jurisdictions, however, address this through different means such as appellate practice, strict rules of evidence or decision making that are strictly enforced, and alternative dispute resolution mechanisms such as arbitration and mediation. These solutions are not sufficiently developed in the COMESA region and disincline investors to cross borders and increase their risks.

4. Recommendations

The goal of the Regional Roadmap analysis was to identify constraints to investment on a regional basis. Although the methodology included examination of specific industries in specific countries, the purpose was not to arrive at specific conclusions and recommendations regarding those industries or countries, but to identify common themes across all industries and countries. This has resulted in a set of recommendations with broad application, which can be applied across national and industrial lines to address investment constraints.

The recommendations have been grouped according to the types of constraints identified. Each of them is derived from the analysis of factors involved in an investor's decision-making process in analyzing return on investment. Many of the constraints have an impact on several of these factors. For example, administrative barriers can increase costs of investment, costs of doing business, and the level of risk in an investment. To avoid the redundancy in addressing these constraints by impact, we have found it more useful to categorize them according to type.

The recommendations, therefore, fall into the following categories:

1. Administrative and Bureaucratic
2. Enforcement and Compliance
3. Finance
4. Information
5. Policy Harmonization
6. Private Sector Capacity
7. Transport

The recommendations flow from the various conclusions regarding investor decisions, with general recommendations followed by increasingly specific options for addressing the problem. At times we have captured the specific industry issues as examples of the constraint or how to remove a barrier in order illustrate more general issues that can be applied across industries. These recommendations are intended to serve as the basis for an action plan by COMESA, and thus are intended to lead to very practical actions that can be taken to improve the investment climate.

1. **Administrative and Bureaucratic Barriers**

a. <u>Restrictions on the Use of Expatriate Staff</u>. Numerous investors complained that it was difficult to bring the management and technical staff they need across borders due unnecessarily strict immigration procedures. The more obstructive restrictions tend to limit the number of expatriates permitted to enter, the period that they may remain in country, and the high expenses involved in requiring all applications to be made in country with immigration, rather then at embassies or consulates where the workers live.

These issues will increasingly need to be addressed as the Common Investment Area adopts policies favoring free movement of labor as well as capital.

I. Case Study: Work Permits

Lithuania

Lithuanian's Ministry of Migration can be considered best practice, in that it uses the tax authorities to confirm and monitor whether an investor has taken up the activities specified in the company formation documents. An effective monitoring system reduces the need for an initial vetting, because officials are better able to identify, and deal with, intentional violators of the Lithuanian Laws as the problems occur.

Countries that do not monitor investors progress must be much more thorough in their vetting and often put investors through a great deal of initial bureaucracy.

By law, the government must issue the Special Visa or notice of rejection issued within 30 days of filing. Latvia has a similar law on it books to process applications within 30 days, however, many investors there disputed whether the process is actually completed in this period of time. By contrast, investors in Lithuania speak highly of the current process and have indicated it to be relatively problem-free

COMESA can encourage an investor-friendly approach to immigration policy. Most of the restrictions on immigration are intended to protect national labor pools and ensure an increase in local employment rather than import of foreign labor. While these are understandable goals, the cost of the restrictions is that many investors cannot bring in the people they need, for the period they need them, and at a cost they can afford, and therefore they simply do not invest at all or do not invest as much. Technicians and management are not fungible commodities, and often are needed to instill corporate culture, corporate procedures, and corporate strategies into the operations of the new investment. This can take years, not just months, and should be left to the investor to decide. Instead of preserving jobs, these restrictive policies can actually have the impact of reducing overall employment by reducing cross-border or foreign investment. Although some ongoing restrictions are justifiable, governments should err on the side of encouraging and facilitating investment rather than controlling local employment.

Specific actions that can be taken by Member States include elimination of "quotas" or limitations on the number of foreign workers to be employed. It may be appropriate to maintain categories (cleaners, for example), but even then officials should recognize that there might be a need to bring in persons from even the "lowest" category to train or demonstrate processes.

Second, Member States should eliminate or reduce the time limits for foreign labor. How long an expatriate employee will be needed to train or transfer technology to local employees cannot necessarily be determined at the outset, and certainly not by an immigration official who does not run the business. Although there may be "abuses" on occasion of allowing a person to stay longer than local conditions require, the impact of this is more imaginary than real. The greater cost is in eliminating the ability of the investors to manage their operations based on business needs, and therefore causing them to take their investments to other regions that do not apply such restrictions.

Member states could also facilitate investment by permitting visa and immigration applications to be made at embassies and consulates abroad. Many investors complained about requirements that all such applications must be made in country, which is less convenient and more expensive.

b. Coordination between Agencies. Investors noted that agencies with overlapping jurisdiction are often not coordinated, resulting in higher costs from duplicative efforts and higher risks in predictability of outcomes. For the Regional Roadmap, the complaints focused most frequently on promises by Investment Promotion Agencies (IPAs) regarding investment incentives that the tax authorities would not recognize. Comparison of National Investor Roadmaps also identified numerous problems in purchase and registration of land as well as applications for licenses and permits.

Jurisdictional issues should be established before investors ever apply for incentives, licenses or other approvals. These relationships should be established by law or regulation, and the rules should be published, available, and adhered to. IPAs must either be given authority to provide enforceable promises to investors, or identify who does have the authority and assist the investor with obtaining enforceable guarantees from that agency.

In the area of customs, investors noted that many countries have various different bureaus or agencies handling different aspects of import/export related transactions. Rather than having separate authorities for import licenses, export licenses, customs clearance, duty payments and other issues, investors suggested that a "one-stop shop" would lower their costs, facilitate transactions, and improve coordination. COMESA should examine the successful IPA model as a basis for encouraging rationalized customs-related procedures.

Analysis of the National Investor Roadmaps indicated that land purchases and leases are fraught with conflicting authorities, duplicative efforts, and complicated processes. Uniform policies and procedures would help to provide a more stable, predictable investment environment for one of the most important aspects. Delays in land registration undermine an investor's ability to invest effectively, increasing the necessary rate of return to cover the expense and risk. COMESA could provide an invaluable service by helping to rationalize the process. This could include working out policies on how to obtain title from traditional and official authorities, including a standard sequence.

II. Case Study: Land Acquisition

Malaysia/Chile/Hungary/Mauritius

In 1998, USAID commissioned a study of the world's leading developing nations in attracting foreign direct investment. Regional leaders Malaysia, Chile, Hungary, and Mauritius were studied for Investor entry, land access and development, licenses, and importing and exporting.

One commonality held by all four countries is the ease with which investors have access to government land for development. Times to acquire land range from 2 weeks up to 6 months. These governments have taken note of the fact that an investor's ability to find and locate on an appropriate site in a timely manner is one of the most critical factors in an investor's choice of country.

Other commonalities are that in all the countries studied, the municipality plays a proactive role in either processing the request or identifying a proper location. The local authorities are often considerably more knowledgeable about available key locations. They have the added motivation (that centrally run ministries often don't have) that the investment will increase the tax base of the region and increase employment.

Licenses and approvals were another area of frequent complaints in the Regional and National Roadmaps, especially with regard to the number of duplicative and redundant forms and procedures required by various agencies involved. This was particularly true with regard to company registrations and subsequent filings that required repetition of much of the information required for registration. Noting that COMESA has already successfully addressed a similar problem in the customs area by rationalizing customs recommendations, COMESA should consider applying those lessons learned to the simplification and rationalization of approval procedures. More specifically, COMESA could develop a standard form and approach for company registrations.

c. Lack of Transparency in Bureaucratic Decisions. Both the Regional and National Roadmaps identified problems for investors in having applications and approvals denied unexpectedly and without any apparent reason. Such denials can be very damaging, not only for the investment affected, but for potential investors who may not be willing to risk a similar fate.

As a general rule of law throughout the world, decisions by government authorities must be based on published laws and regulations, must be written, and must provide the reasons for the decision. Otherwise, the system can be easily manipulated or corrupted, or at least give the appearance of manipulation or corruption, while creating an unacceptable atmosphere of uncertainty.

COMESA can address this by establishing standards, forms and procedures for issuing decisions to deny applications. The procedures should include some form of reporting to national governments, the IPAs and to COMESA itself, so that performance can be monitored. In addition, establishment of transparent procedures will build investor confidence that the rule of law is being applied to their investments.

d. Unacceptable Delays in Duty Drawback Schemes. A number of countries offer refunds or drawback of import duties for imports used in the creation of export products. Investors complained that in some places the procedures are so complicated and the delays so extensive that they sometimes just forego the process altogether. This eliminates or diminishes a needed export incentive and depresses the profitability of the firms.

Building on the successful customs document simplification program, COMESA should work with Member States to standardize and simplify the processes for obtaining drawbacks or other benefits related to import and export tariffs. This could start with an examination of the causes of delays (which could include bureaucratic complexity or simply a lack of revenues), followed by a plan for reducing each type of delay.

e. Non-Recognition of Licenses from Other States. Many countries do not accept licenses issued by other authorities as valid, and require cross-border investors to go through complicated or expensive licensing regimes in their own states, rather than provide some sort of full faith and credit to the decisions by competent authorities of their neighbors.

COMESA should consider creating a regional licensing regime to simplify cross-border trade and investment. This could begin with the formation of licensing committees to determine the requirements for such recognition and to determine the feasibility of at least some registrations being made on a regional basis.

f. Poor Quality of Service from Government Officials. Investors complained of poor service from government agencies, including customs, immigration, licensing authorities, and others. The complaints centered on two problems – attitude and technical knowledge. Attitude may be more difficult to address, but it must be addressed.

COMESA can create regional standards for customer service, including training modules, standards and procedures for government functionaries who work with the public. The principle purpose would be to move agencies into a role, undergirded by an attitude shift, in *facilitating and promoting* investment instead of trying to simply *control* it. A campaign to promote better relations between the public and private sector based on partnership principles and goals could be instituted. This should include some form of feedback opportunity for customers to compliment or complain about performance.

III. Case Study: Building Permits

Tanzania

The story of Tanzania's building permit approval process, as measured in the capital city Dar Es Salaam, is one of remarkable transformation. Previously, the process was backlogged for several years. This was a significant deterrent to investment, and encouraged the building of illegal, and in many cases unsafe structures.

The Dar Es Salaam City Commission has worked to make the current process move more quickly and smoothly. The Commissioners now meet weekly, which has been an important step in reducing a backlog of applications from previous years. Once the application is submitted, various departments within the City Commission will examine it. Town Planning will ensure that the proposed activity is in line with zoning and plot coverage restrictions as well as checking the validity of the title. City Health officials will examine the plans in terms of water, drainage, sewerage and other health issues. The City's architects and engineers will check the plans to ensure that the proposed design is structurally sound.

By law, the delay for approving building permits should be less than 60 days. City officials state that most applicants now face a delay of one to two months, with a maximum of three months. The delays have been reduced in recent years as approvals are now granted by Commissioners, who meet every Friday to decide such issues.

There has been a shift of responsibility to the various commissioners to come to the meetings prepared to either approve or give valid reasons why they don't approve applications. In many cases, architects and engineers will work directly with the various commissioners' offices to iron out any problems that might be incurred during the meetings.

Lessons can be taken by other countries from this example. In particular, it should be noted that the various commissioners are expected to come to the meeting prepared to give their recommendations on projects (for approval or rejection) on the date scheduled. This forces the various departments to be timely in their analysis.

COMESA may wish to form one or more committees or working groups based on priority areas – such as licensing boards – to set benchmarks and standards of performance in processing documentation.

The other complaint was that many officials who were vested with the authority to approve or disapprove various business actions did not have a sufficient business background to analyze the facts properly, and thus denied applications or mischaracterized facts to reduce benefits. This was true of tax authorities who did not fully understand the underlying accounting rules, building permit authorities with insufficient engineering backgrounds to approve or disapprove blueprints, and even environmental officials with insufficient scientific training. Another complaint was that in some countries there were inappropriate technical approvals required, such as immigration officials reviewing factory site plans as part of the process of deciding whether to grant expatriate work visas.

The consequences of technical incompetence are serious, resulting in both inappropriate disapprovals of valid applications and approvals of invalid requests. Because of the variety and number of approvals and licenses granted throughout the various industries, it may not be feasible for COMESA to attempt to directly affect each of them. Instead, COMESA might consider establishing subject matter groups, headed by different countries, to determine on an industry basis what licenses and approvals are needed, and what qualifications are required for employment of government officials. Inspectors, for example, must have a minimum of training and experience before they are entrusted with inspections.

For inappropriate use of technical evaluations, the complaint seems mostly to be focused on immigration. To address this requires a study of what is currently required by Member States, followed by an evaluation of what is actually needed in order to identify items that can be removed.

g. Labor Issues. The National Investor Roadmap analysis identified excessively protective labor policies as a constraint to investment, and this is certainly a constraint to cross-border and regional investment. The problem is that many of the labor laws attempt to protect employees from losing their jobs without any apparent understanding of the nature of business cycles and economic factors underlying the business decisions of hiring an employee. The principle result is that it is extremely difficult and expensive to dismiss employees that are no longer needed. Consequently, employment itself is a very risky business, and investors must exercise extreme caution in determining levels of appropriate staffing. More to the point, these burdens restrict the ability of investors to respond to market forces and result in fewer workers being hired.

IV. Case Study: Registration

South Africa

South Africa has perhaps the least imposing registration processes of any of the countries studied. Procedures are completed quickly, many other registrations are automatic (despite using manual techniques of sending copies of applications rather than computerization), and in many cases an investor is permitted to trade while registration is in process.

There are three main types of registration in South Africa – companies, close companies, and branch offices of foreign companies. Company registration, at the time of study (1997) was completed typically within 3 to 5 days. Closed companies, a new form of company for small indigenous businessmen, was fairly backlogged and could only be formed within 2 weeks.

Upon completion of business registration procedures with the Office of the Registrar, SARS is notified by the Registrar and the business entity is automatically registered as a Provisional Taxpayer and issued a registration number. For income tax purposes, every enterprise must appoint a “Public Officer” to represent it in all dealings with the Revenue authorities, including annual returns.

Those required to register for VAT must do so before trading commences. The company must have an active bank account before registering. The Receiver can issue a registration number within one to two days, after which trading may commence. Full approval requires two to three weeks.

Employers must register with the local Receiver, using form IRP 101. Employers are issued a registration number within one to two days, though final approval requires two to three weeks. Trading and hiring may commence immediately, though. The Receiver must be notified of all new employees.

One example is useful here. There is currently an overwhelming demand for American flags, and it has completely outstripped supply. The major suppliers are oriental textile manufacturers, with the bulk of American (and all other flags) made in the Far East. A flag manufacturer who wants to capture this opportunity might consider hiring workers to work additional shifts in order to produce more using the same equipment. Theoretically, a manufacturer could triple the number of employees while the demand lasts. In many COMESA countries, however, the manufacturer might simply decide to pay a little extra overtime and skip the opportunity, because it would be extremely difficult to dismiss the employees when the demand passes in a few months. Jobs and revenues are regularly lost by laws intended to protect and encourage employment.

COMESA should consider working with the International Labor Organization and management organizations to review existing labor laws and propose standard rules for employment in the region. The need to protect labor must be balanced against the need for employment, recognizing that each protection has a cost, and not all costs should be born by the employer.

2. Enforcement and Compliance

Investors frequently complained of problems of compliance and enforcement with laws, regulations, and even private sector contracts. Poor enforcement reduces predictability and increases costs of doing business. COMESA is already organized to address these issues, in part through the Court of Justice and through other programs. Different aspects of the problem are presented below.

a. Lack of Transparency in Administrative Decisions. This has been addressed above as a bureaucratic constraint, but has more levels to it. First, transparency is a legal issue – laws determine the basis and processes for decision making. To inspire investor confidence, the rules must be clear, rationale, and public, and the decisions must be written and based on laws. COMESA countries should adopt internationally accepted standards and procedures for administrative decisions. COMESA could start this process by identifying the rules and establish a policy for Member States.

Second, a system of transparent rule making must be backed up by a system of appeals. Not all decisions are correct, and there must be a way for an investor to challenge the denial of an application. COMESA should appoint examine the appeals systems within the Member States to determine where and whether investors have satisfactory remedies. This study may indicate whether the Court of Justice should be included as a court of final appeal for such decisions. At the very least, the study should result in recommendations for standard or preferred procedures.

Finally, it should be noted that transparency requirements are essential for fighting various forms of corruption.

b. Inconsistent Application of Customs Duties. COMESA has already scored significant successes in simplifying the customs regime by reducing documentation, tariff bands and tariffs themselves. However, there are still problems with uneven application and enforcement of duties. These variations can result in unexpected costs, and unfair competition based on manipulation of tariff costs.

The first need is for proper training of customs officials, which can be handled under COMESA's customs programs, and will include the application of harmonized tariff standards. Assuming improvements here, however, there will still be opportunities for abuse.

Problems in uneven enforcement come to light in two ways. First, some investors find that their goods are being mis-categorized, based on experience elsewhere, or that the same product at different times and places is receiving different treatment. This requires a meaningful system of appeals. COMESA should examine the process for appealing decisions and help to develop standards for resolving such differences.

Second, investors discover that their competitors are able to substantially undersell them, and know that the only significant cost variable is customs duties. In this case, investors need a way to determine if in fact this is the case and to challenge it. COMESA should contact the International Customs Organization for advice on how such issues are handled internationally, in order to capture proven best practices. Based on work with the ICO or other organizations, COMESA should work through its customs programs to ensure that proper mechanisms are in place.

Third, COMESA should determine whether the privatization of customs services is a valid option for the region. This has recently been done in Mozambique, where customs services are now run under contract with Crown Agents of England. COMESA should study this program carefully for applicability, then make recommendations based on the study.

c. Lack of Mechanisms for Reporting Corruption. Although there are widespread complaints of various levels of corruption, there are few ways for investors to deal with it. Where corruption is systemic, it does no good to report it, and can in fact result in punitive actions taken against the company or individual who dares to complain. Because of this, victims of corruption may wish to remain anonymous at first.

COMESA is a natural contact point for complaints about corruption. It is independent and separate from the bodies being accused and has no stake in the outcome. Therefore, COMESA should form a regional committee of national agencies, NGOs, and representatives from international organizations to address issues of corruption.

COMESA should provide a means to report corruption anonymously, including, perhaps, an Internet website, a hotline, and a mailing address. Using information from the reports, COMESA can identify trends and inform Member States of reports, as well as provide support to national anti-corruption units. The Internet site should include information about what corruption is, who has jurisdiction for such complaints in each country, how to report it locally, plus a standard on-line form for reporting incidents anonymously to

COMESA. The form should include standard information such as time, date, place, facts, nature of corruption, parties involved, specific parties being accused, etc.

d. Lack of Confidence in Local Courts.

Many foreign investors perceive local bias against them in the courts and thus do not bother to bring complaints. They believe that appealing a biased decision will only result in another biased result. Whether the perception is based on verifiable fact or rumor, the result is the same. Consequently, an "honest broker" is needed to hear appeals from suspect cases.[1]

The Court of Justice should consider how it can meet this need. If the court were to hear appeals based on bias, it could address the issue without unnecessarily becoming a dumping ground for all appeals. The Court should study propose jurisdiction for such cases and basis for hearing a case. In other words, the case should focus on bias and the facts relating to bias, and should not necessarily relate to the entire case. Rules could provide for evidence, such as failure to provide a written opinion that would place the burden on the courts to prove that they were unbiased. Indeed, because of the amount of money involved in such cases, the Court could assess fines against a court if bias were proven, and use that to defray costs. Such fines would also act as an incentive for a country to clean up its court system.

e. Poor Enforcement of Private Sector Contracts. Numerous investors, especially those involved in credit, complain of poor support from courts when trying to enforce contracts. Sometimes the cost of pursuing the complaint is higher than the amount in questions, or the courts simply issue biased opinions (as noted above) When contracts cannot be enforced, investors find other methods to ensure compliance – such as guarantees, possessory pledges and other stopgap measures – all of which raise transaction costs, as well as just foregoing those types of transactions that cannot be enforced. This is particular damaging in credit transactions, where inability to collect loans results in loans no longer being made.

There are several issues involved, leading to several suggestions. First, the cost of litigation is unnecessarily high in some countries. In Zambia, for example, there is no cost-appropriate system for dealing with smaller claims through the courts. This is in part due to unnecessarily complicated procedures, requirements that a lawyer be used (which is not always necessary in small claims) and legal fees.

The Court of Justice should consider establishing a program to simplify procedures for enforcing common commercial transactions. This should include standardized forms, confessions of judgment, and even a "fast track" approach to ensure immediate attention

[1] It is interesting to note that this fear of bias is one basis for the U.S. system of state and federal courts. Non-residents may sue in federal courts or move actions in which they are sued to federal courts based on a belief that there will be less bias in the federal system.

from the courts. Proof should be very simple, where possible. For example, suits for non-payment focus on one issue only – whether the defendant paid – and there is no need for complicated findings and procedures. (As a safeguard against bias, there should be a mechanism for appealing to an impartial arbiter, as discussed above.)

Second, some of the problems are related to poor training of judges. Sometimes judges do not understand the issues being presented, and consequently make poor decisions. The Court of Justice, in concert with commercial associations such as chambers of commerce, or even regional business schools, should appoint a task force to identify the most common types of transactions, then design a curriculum that could be used throughout the COMESA region.

Third, the business community often prefers to use alternative dispute resolution instead of the courts. Such procedures exist at higher levels (almost universally with respect to larger claims of foreign investors), but not always at the low end. Frequently, such services are offered by business associations who can build a strong reputation for integrity and become an essential support to commercial transactions. The Court of Justice should commission a proposal for identifying and working with business associations to establish ADR programs to handle commercial claims.

3. Finance-Related Constraints

The cost and availability of all types of finance, including trade, purchase, export, working capital, and other loans were frequently noted by investors as serious constraints. COMESA is well aware of this, and has successfully supported the PTA Bank, among other programs. These are certainly filling important investment-related functions, but the demand for more and different financial services far outstrips the capacity of the PTA. In addition, some of the needed forms of finance are not yet supported by the national legal regimes. The cost of capital is still very high, often greater than 20% annually, in part because of risks of non-payment and insufficient supply of financing.

a. Lack of Secured Financing Products.

One of the foundations underpinning the credit industry in much of the developed and rapidly developing world is security. This includes mortgages on land and immovable property as well as pledges on movable property. This security lowers the risk to the lender, permitting the lender to reduce interest rates and make more capital available. For most COMESA countries, the practice of and infrastructure for secured lending are missing.

COMESA should lead a regional program to expand credit through the establishment of a collateral lending regime. The program should be harmonized on a regional basis to ensure that individual countries do not adopt systems that hinder regional development. Approaching this on a regional basis would greatly lower the costs – as compared to the country-by-country, separate programs being implemented slowly in regions such as the

Balkans. This should start with a survey of existing laws on property rights and banking practices. The laws can be analyzed to determine common bases for establishing a new regime, then followed by a proposal to implement a region-wide, harmonized secured lending system. COMESA could then also lead the efforts to obtain financing and assistance for implementation of the project. Once implemented, a functioning collateral law system permits financing of equipment, inventory, warehouse receipts, crops, livestock, accounts receivable and numerous other commercial transactions.

b. Lack of Secure Title to Property

National Roadmaps identified serious problems with title to land. Because land is the primary asset used in secured lending, this has a tremendous impact on the ability of investors to obtain capital (or even to lower their risks sufficiently to make an investment).

COMESA should establish a commission on land and property rights. The commission could identify and categorize the problems in land, then suggest solutions based on practices in leading COMESA countries, other African countries, and other successful systems. The focus of the work would be to establish ownership rights and issue titles reflecting those rights.

c. Disjointed Programs for Finance.

There are numerous activities in the region to support growth of credit. Donors such as the World Bank, USAID, the European Community, and many others are attempting to develop micro-lending, improve trade finance, upgrade banking practices, etc. Though these entities are well known on a regional basis, their projects tend to be known on a local basis, and seldom outside of a country. Often the programs are not coordinated, which can lead to conflicting strategies.

COMESA should act as the primary clearinghouse for information regarding such programs. Once known, COMESA would be a focal point for both investors and donors who want to know what is happening in the region in this area. COMESA should consider requesting that donors notify them of all programs in the region, and develop a standardized form for such information along with a point of contact and website. In addition, COMESA should request that copies of all project reports be sent to COMESA by the implementers as a project requirement. This would permit COMESA to capture the wealth of information produced by these projects and build both a library and database.

The purpose of this is not to give COMESA decision-making authority over donor programs, but to forge a better partnership, improve coordination, and provide information in a transparent manner to all interested parties. Over time, COMESA might wish to take a support role to assist its members in obtaining and negotiating such projects.

4. Information

Of all of the recommendations in this report, it appears that the one in which the greatest gains can be achieved at the greatest likelihood of success is by dramatically increasing the information flow from COMESA to the investment community both within COMESA and abroad. COMESA has made several efforts to communicate its programs and policies, most notably recently though road shows by the Trade Department, but investors interviewed were clearly ignorant about many of the advantages of COMESA and the programs it offers.

Most managers are inundated with information on a regular basis. COMESA competes for desk space with other trade organizations such as SADC, ECA, and such programs as growth triangles, proposed trade corridors, and other bilateral and multi lateral trade agreements. While keeping up with the huge number of agreements is difficult enough, some countries have randomly applied tariffs and duties temporarily in certain situations. Many managers simply deal with this confusion by ignoring it.

The lack of communication between COMESA and the private sector can be witnessed not only through the lack of anticipated growth in cross-border investment, but in the lack of private sector support for the trade policies. It seems that the most vociferous of the private sector are those that have benefited from levels of tariffs and non-tariff barrier protection. Surprisingly, those companies that have either benefited, or are in a position to benefit have not provided a counter balance in the form of support. In many cases this can be ascribed to a lack of understanding of the opportunities.

But questions remain as to how to distribute information in a manner in which it will be consumed by the intended private sector targets and retained by them. As mentioned earlier, managers are inundated with information. COMESA must be aggressive in attacking this problem, and cannot assume that the private sector will seek it out over other programs that are constantly being represented to management.

a. Image Building

As identified earlier, one of the four components of the investment decision is risk, and risk is what is perceived, regardless of whether the perception is equal to reality. Incorrect perceptions are purely a function of the absence of information, or the presence of incorrect information.

Member States invest considerable sums of money on producing marketing materials that promote their individual countries as investment destinations. Of course, a central component of these presentations are the messages of stability and safety in investment. However, investors are now very aware of stability issues in neighboring countries and do not make risk decisions purely on the basis of an individual country's track record. Therefore, COMESA, through its Regional Investment Agency, should produce materials touting the history of the region and the policy stability that many of its Member States have enjoyed over the past decade. While some Member States have had military conflicts and others have gone through political upheaval, the vast majority has been stable economically. This message must be crafted region-wide.

b. Market Information Studies

There have been market information studies conducted on many levels, by many different organizations including Member States governments, Western Countries governments including the United States and Britain, manufacturers' associations, and others. However, the average investor has limited access to these studies. Some organizations, notably MEDIA of Mauritius, maintain an extensive database of market opportunities in COMESA Member States. Most do not.

COMESA can act as a library for these studies. It will take a joint effort to effectively build this library and distribute the information via Investment Promotion Agencies around the region. On the one hand, Member States IPAs must come forward with all available studies to be placed with the COMESA Secretariat. The Secretariat must also be active in cataloguing and redistributing existing studies. It must also search all relevant sources including the Internet for other studies that exist.

These studies can be distributed through a number of methods. One is to reproduce them on CD-ROM to be kept within the facilities of the Investment Promotion Agencies. These CD-ROMS can also be sold to the private sector to recover some of the costs incurred in establishing these operations.

The studies can also be placed on COMESA's website. However, many members of the private sector are not aware of COMESA's presence on the Internet, and this method will only be effective should COMESA actively promote the existence of its site.

COMESA may wish to turn to the private sector by privatizing this function. As opportunities to grow and invest increase, the demand for information will grow exponentially. There are many media organizations around the world that would be capable of managing the collection and dissemination of data around the region. COMESA could interact with a company in a variety of methods by either promoting it as a regional investment opportunity or engaging in a build-operate-transfer type solution.

c. Regional Tenders

Some investors felt that they were capable of supplying goods to neighboring Member States governments, but without a physical presence in the country, find it next to impossible to know the existing tenders. Tenders are often published in government bulletins that rarely leave the home country.

A service that could maintain a presence in each member state (or maintain a network of individually owned media outlets) could gather and disseminate information to the private sector rapidly via email or by posting information on a website on a subscription basis. It is unlikely that the secretariat is equipped to establish such an operation internally, but should promote such an investment to potential investors in the media business.

d. Defining COMESA vs. different trade organizations.

As noted earlier, managers in the private sector are inundated with information about various bilateral and multilateral agreements, both real and proposed on a daily basis. A quick scan through the various publications indicate that many are not easily read and not written to the needs of a businessperson. Often information is created by members of the public sector or former members of the public sector that have little or no understanding of the amount of information an investor faces.

COMESA must view itself in competition for the attention of its investors with other trade institutions and agreements. It must differentiate its message, create easily retainable concepts, and market this information in the manner of any other organization that is required to compete in order to survive.

In order to be successful at the above, it is recommend that COMESA engage the services of a professional media and marketing agency that understands how to gain access to the very limited attention span of private sector managers. This professional organization should ideally be closely familiar with the needs of the private sector and be somewhat familiar with the various trade programs that are ongoing in the region. They should be called upon to define messages, and means of dissemination. It would also be valued if, in the process of promoting COMESA and its programs, that the website be actively promoted.

e. Lack of readily available information on tariffs, laws, and regulations

COMESA owns the perfect distribution method to address the concerns raised by investors on the availability of laws, regulations and tariffs; its website. However there are constraints that have not allowed this vehicle to serve its purpose and address all of the concerns raised.

The COMESA Secretariat has not, to date, aggressively sought out documentation from Member States to populate the website with data on investment laws and regulations. This is a task large in scope and resources, and may be beyond the Secretariat's immediate means. Given the current level of resources, it would take a concerted effort by Member States to supply the Secretariat with all of the relevant documents for electronic publication. Even then it is not clear that the Secretariat would not be overwhelmed and unable to publish in a timely manner.

Throughout this section of the recommendations, mention has been made of the need to upgrade COMESA's ability to gather, sort, and disseminate information in a timely and effective manner. This is a role, of course, of the Secretariat, and it will require a significant upgrade in their resources to address such a concern.

Currently, the COMESA website is being maintained by the same department that handles COMESA's internal information systems management. While the skills that are necessary to maintain the two are similar, this report suggests that the activities and goals are, in fact, very distinct. It is therefore recommended that the website, and any promotional activities thereof.

f. Defining the Common Investment Area

As noted earlier, the concept of a Common Investment Area is new to investors in the region. While this is not surprising given that the concept has not been operationalized within COMESA, it misses an important opportunity for private sector participation in the critical design stage of the proclamation.

It is therefore recommended that as part of any marketing plan, COMESA promote the fact that it intends to become a CIA in an effort to request feedback from members of the private sector in the region.

5. Policy Harmonization.

COMESA is and has been committed to the harmonization of policies, laws, tariffs, and practices in the region on a number of fronts. As a result, it is already highly experienced in taking on harmonization tasks. A number of recommendations have been made elsewhere in this report with respect to harmonization of some specific issues. The recommendations below did not fit comfortably into the other categories.

a. Ad Hoc Tariffs. A number of investors in the Regional Roadmap and National Roadmap interviews complained that application of tariffs is not always predictable or reliable. Ad hoc and inconsistent application increase costs and risks and create an uncertain investment environment. Although some of the problems will disappear as the FTA and common external tariff regimes are implemented, there are still valuation issues that will survive into the new system.

COMESA would do well to ensure that a mechanism is established to deal with such problems in an effective and timely manner. An initial step would be to identify trends and locations where the problems are worst. One of the existing committees on trade and tariffs could handle this, or a new one could be set up that could establish a reporting mechanism for investors. This would require heavy advertising among freight forwarders, import/export associations, and even the customs service, and might best be done through an internet reporting site and hotline.

Once information begins to come in, COMESA could let competent authorities in the Member States know about the problems so that they could address them. In addition, COMESA could use the information to identify subject areas in which there are problems and design courses for customs officials to address them. In addition, the COMESA committee should make findings public through news releases and web articles to create public pressure for change or to celebrate successes for those who correct problems.

Finally, COMESA should encourage use of the Court of Justice to provide unbiased judgments on the propriety of tariff decisions, following appropriate appeals to local authorities.

b. Variations in Environmental Laws.

Several investors (particularly in the leather industry) noted wide variations in the content and enforcement of environmental laws and policies. This has an impact on regional investment patterns. In addition, excess regulation discourages investment, while insufficient regulation has serious environmental and social consequences.

COMESA needs a regional approach to environmental regulation. The starting point could be the creation of a commission on Environmental Regulation whose duty it would be to develop a regional environmental code, inventory the environmental enforcement resources in the region, create enforcement guidelines and generally oversee environmental issues.

c. Used clothing imports.

Used shoes and clothing imports were noted throughout the Regional Roadmap survey as the most important factor in the ability of local manufacturers to capture a significant share of the local market. Indeed, representatives of both industries admitted that they simply could not compete, and thus produced for the export market, or simply did not invest in certain types of production for the local market.

Some countries have addressed this by forbidding or heavily taxing these imports to permit local industry to develop. For example, Ethiopia prohibits importation of used leather shoes in order to have a local shoe industry. We believe that most countries are making the correct response by permitting importation of used shoes and clothing, however, and recommend that COMESA officially encourage this healthy market-oriented approach.

Africa is home of some of the world's poorest consumers. They do not buy used clothing out of preference, but because they can afford it. Much of the clothing is of very high quality and it meets the needs of an extremely high percentage of the consumer market. Cost/benefit analyses suggest that the costs of causing all of these consumers to pay more for their clothing is not justified by the benefit of employing a few thousand people through protective tariff structures. Moreover, used clothing purchases are a function of wealth. As incomes increase over time, most consumers will shift to new clothing. For the time being, we recommend that COMESA support this free market approach as an official policy.

V. Case Study: Free Zones

Dominican Republic

The Domincan Republic has used free zones extensively to attract foreign investors. The free zones are privately run. The Dominican Republic has created Law 8-90 to provides numerous customs and tax incentives including 100% exemption on:

- Income tax;
- Construction tax;
- Taxes on the founding of commercial societies;
- Import taxes, including those for machinery and equipment;
- Consular taxes;
- License taxes;
- Tariffs and customs duties;
- Export or reexport taxes.

These exemptions apply for 20 years in the border free zones and 15 years in the free zones in the remainder of the country.

Most foreign companies operating in the Dominican Republic are located in one of country's 34 free zones. The operators of the Free Zones have acted as private investment promotion agencies for their own properties. They provide many services for their investors including facilitating many of the government processes. It is considerably easier to set up a company within a free zone than it is outside of a free zone – an investor in a free zone may be able to cut the time of registration from several months to several days.

Dominican incentive laws were largely eliminated by the Tax Code introduced in 1992. The only remain fiscal incentives in the Dominican Republic are those granted to free zones. Law 8-90 allows for three types of free zones:

- *Industrial or Services Free Zones* for manufacturing of goods and the provision of services;
- *Border Free Zones*: because of their location in economically depressed areas, companies are provided with special incentives that are delineated in Article 29 of the Free Zone Law;
- *Special Free Zones*: these free zones are located in areas where companies would have easier access to critical resources.

d. Differing Transport Policies.

COMESA is well aware of the need for harmonized transport policies, and has been working on such policies for years. Those areas which have produced complaints are already being addressed or on the agenda. Much of the remaining harmonization work focuses on negotiating solutions with SADC.

Rather than reiterate investors' comments about items that have been targeted already, we recommend that COMESA also focus on regional training initiative for enforcement agents involved in transport to ensure shared understanding and complementary practices.

In addition, COMESA should establish a regional base for settling unresolved complaints of non-compliance and take jurisdiction to hear and decide those complaints. Enforcement of the rules is as important than the rules themselves. COMESA should establish a system for ensuring compliance.

e. Limited Approach to Investment.

The National Roadmap analysis shows that many laws related to investment promotion and investment incentives suffer from a restricted definition of "investment". Instead of recognizing the different phases and types, the laws focus on high ticket, fixed asset investments, thus leaving out incentives for early phases leading to fixed assets, and completely missing most investment in service industries.

COMESA should take the lead in changing the presumptions and understanding of investment. This can start by working with IPAs to develop a program for encouraging all forms of investment at all levels, and reducing costs. A committee of IPA representatives could analyze incentives to determine those that could be offered more broadly. Moreover, the committee should create a strategy for targeting investment in the service industry to capture opportunities based on globalization and technology, such as offshore processing for credit card companies, for example.

g. Privatization.

State involvement in private sector activities through state owned and parastatals has an impact on attraction of regional investments. Investors tend not to try and compete with state firms because those firms have competitive advantages not based on market considerations. An investor interested in making an investment on a regional basis will look for countries that are not neighbored by state-supported industries.

COMESA should establish regional policies on privatization to encourage governments to disengage from activities better served by the private sector. A committee should conduct or commission a comparative study of existing privatization initiatives and progress in order to identify relative progress. From there, a timetable should be established, in a manner similar to that used for entering the FTA and establishing the single external barrier, then support, encouragement, and pressure should be brought on recalcitrant governments to disinvest.

6. Private Sector Capacity

The private sector needs to be strengthened not only to support regional investment but for its own benefit. Investors have pointed out a number of areas in which private sector weaknesses increase the cost of doing business in the COMESA region, making it a less attractive region. Moreover, these deficits lower the overall development of each country.

a. <u>Local Educational Programs Not Producing Needed Skills</u>. A number of COMESA countries have invested relatively large amounts in improving their educational systems. Even in these countries, however, investors complain in the National Roadmaps that the skills being taught do not sufficiently meet the demands of the business world, so that they must invest unnecessarily large amounts in training of employees for basic skills, or simply bring in foreign labor, where possible, instead of hiring locally. Although all firms must provide some sort of training because of their own unique internal requirements, investors find that the basic education does not fit their entry-level needs.

COMESA and the Member States can work with investors to identify educational gaps that can be addressed by changing existing programs. There is a need for public-private partnership in education. COMESA can lead this effort.

COMESA should continue to establish and maintain working relationships with private sector associations who will be responsible for identifying educational and training needs not adequately addressed by existing institutions. Within these relationships, regional institutions – universities, training centers – can be identified for specialized courses and degrees.

Through SADC's programs that have targeted various industries, it may be that some of these exercises are already being undertaken. COMESA should first catalog all of the other efforts to improve the private sector through education programs by offering opportunities for members of the private sector from Member States to participate in programs not normally available to them.

b. <u>Lack of Quality Standards throughout Region</u>.

Few industries are consistently producing to international quality standards. Most of the metal products and leather processing studied were below standard for export, even when geared toward export markets. Often this is due to ignorance of the market requirements.

Working through existing ISO and quality program structures, COMESA should continue the work funded by the European Union to strengthen private sector associations to provide members with information and feedback on quality. This should be coordinated with investment promotion agencies, as foreign investors both bring knowledge of such standards and require higher level production. Together, they should design systems for obtaining and disseminating this information.

COMESA can also encourage industry associations to develop and provide systems for certifying quality. For example, LLPI or ESALIA could provide certification that hides meet a certain level of quality and are properly sorted within the quality categories. Over time, this seal of approval would actually increase the value of the products. Fees generated would support the associations and be recouped by the exporter through better prices.

c. Lack of Knowledge on Agricultural Inputs and Practices. Agricultural producers in the oilseed sector are using low quality seed with inferior oil yields, thus obtaining lower returns on the same work required for better seed, and lowering the quality of supply in the oilseed industry. There are indications that the oilseed sector is not alone in this problem.

COMESA should create programs to strengthen agricultural extension services and agricultural associations by obtaining and disseminating information on improved seeds and practices. This information may have to be linked with access to finance, as many farmers may not be able to afford the improved varieties without agricultural credit. Forming regional associations to support national groups and work with ministries of agriculture will be needed.

At the same time, COMESA should issue strong policy statements about governments staying out of the sale of seeds. Only the private sector provides the possibility of sustainable growth in the actual provision of seeds to the market. There are numerous examples of government seed programs destroying the quality of seeds available in the local market.

COMESA website can also establish information links in its clearinghouse role by providing access to agricultural information through extensive hyperlinks on its on sites. These links should be to national, regional, and international industry groups and sources of agricultural information.

c. Lack of National and Regional Market Price Information.

Producers get little information on upstream pricing and thus misallocate resources into lower value crops and practices. This has an impact not only on their welfare, but also on upstream agro-industry that depends on good downstream production.

COMESA should support the establishment of local, national and regional market information services that provide farmgate and export prices on agricultural commodities. More importantly, COMESA should begin to develop a strategy for establishing regional commodity exchanges. In the meantime, COMESA can establish or support websites for market information.

d. Lack of Coordination between and Knowledge of Donor Training Programs.

As noted in the finance section, there are numerous programs in the COMESA region supported by donors, but often there is no knowledge of these outside of the individual countries. Most training programs are nationally based, but could have regional implications.

As recommended on finance, COMESA should as a clearinghouse for information on private sector training. This should include having donors provide COMESA with information on the programs as well as reports, materials and curricula developed for the programs.

e. Insufficient Capacities for AGOA.

Many firms cannot take advantage of AGOA due to capacity constraints. They simply cannot produce in the quantities required by the American market.

COMESA can play a role by encouraging cooperation between small businesses. This can be done in collaboration with the IPAs and should include a mechanism to introduce companies to each other, identify producers, and ensure dissemination and adoption of quality standards.

f. Insufficient Private Sector Input into Policy.

The private sector bears the entire impact of policy decisions but has little advance input on their direction. In many countries, only elites have the ear of government, and though they can sometimes influence the direction of policy very effectively, this results in uneven treatment, unfair advantages, and an uneven playing field.

COMESA should work to establish formal, institutionalized mechanisms for public/private sector dialogue, vetting, and feedback. As a starting point, COMESA should draft a regional policy and model law that requires timely and meaningful opportunities for the private sector to comment on laws in each country before they are adopted. (It's much easier to change a bad draft than amend a bad law.) In addition COMESA should support the establishment and growth of private sector organizations to speak for their members, develop policies, and lobby governments for change.

Finally. COMESA should examine its existing programs and policies on private sector input to see if they can be improved, perhaps by creating permanent private sector representation in COMESA committees, coupled with a commitment from investors and associations to provide consistent input.

7. Transportation

As noted previously under the section on harmonized policies, COMESA has a number of programs to address problems in the transportation industry and road networks. There is no need to reiterate those issues, even if investors raised them as complaints. On the other hand, there are some areas that COMESA might consider wish to move to higher priority.

a. Border Delays from Multiple Crossings. Despite simplification of documents, procedures can still be very complicated or difficult. Border crossings create duplication of inspections and processes.

COMESA should consider creation of single-stop borders, with customs and immigration from adjoining countries working together. COMESA should develop a pilot project, then monitor and disseminate results.

2. Bond Guarantee Scheme

There is already a bond program, but the approach has been to institute the scheme for the entire region at one time. However, user confidence and interest so far have been low. This could be due to a lack of awareness, market conditions (not all industries have the scale needed to participate in this program) or a lack of confidence.

COMESA should consider focusing initial efforts on a single transportation corridor, such as the Mombassa-Kampala highway. By creating success stories, COMESA could build demand and confidence to roll the system out to other important transportation corridors.